



# **NAVAL POSTGRADUATE SCHOOL**

**MONTEREY, CALIFORNIA**

## **THESIS**

**OUTSOURCING, MANAGING, SUPERVISING, AND  
REGULATING PRIVATE MILITARY COMPANIES IN  
CONTINGENCY OPERATIONS**

by

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September 2010

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**OUTSOURCING, MANAGING, SUPERVISING, AND REGULATING PRIVATE  
MILITARY COMPANIES IN CONTINGENCY OPERATIONS**

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## **ABSTRACT**

This thesis examines the utilization of private military companies (PMCs) by government agencies of the United States in contingency operations in Iraq and Afghanistan. The aim of this thesis is to investigate the roles that PMCs play in current contingency operations, and to analyze how PMCs can become more useful instruments in contingency operations if they are properly outsourced, managed, supervised, and regulated. In this regard, this study largely rests on transaction cost economics to explain the logic of outsourcing from governmental agencies' perspectives. On the other hand, principal-agent theory and new institutionalism provide the theoretical basis of using effective oversight mechanisms to exert better control over the activities of PMCs in contingency operations. This thesis recommends the United States, Iraq, and Afghanistan use the Montreux Document as a guide to better regulate PMCs in contingency operations.

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## **LIST OF ACRONYMS AND ABBREVIATIONS**

AAA	Army Audit Agency
ACOD	Armed Contractor Oversight Division
AO	Area of Operation
CACI	California Analysis Center Inc.
CBO	Congressional Budget Office
CEO	Chief Executive Officer
CO	Contracting Officer
COR	Contracting Officer's Representative
CPA	Coalition Provisional Authority
CRS	Congressional Research Service
DCAA	Defense Contract Audit Agency
DFARS	Defense Federal Acquisition Regulation Supplement
DoD	Department of Defense
DOS	Department of State
EO	Executive Outcomes
FAIR	Federal Activities Inventory Reform Act
FAR	Federal Acquisition Regulation
FPDS-NG	Federal Procurement Data System-Next Generation
GAO	Government Accountability Office
ICRC	International Community of Red Cross
ISAF	International Security Assistance Force
ITAR	International Transfer of Arms Regulation
ITGA	Islamic Transitional Government of Afghanistan
KBR	Kellogg Brown & Root Company
LOA	Letter of Authorization
MEJA	Military Extraterritorial Jurisdiction Act
MOU	Memorandum of Understanding
MPRI	Military Professional Resources Inc.
MSP	Military Service Provider
NATO	North Atlantic Treaty Organization

NDAA	National Defense Authorization Act
NGO	Non-governmental Organization
NPS	Naval Postgraduate School
NSP	Nonlethal Service Provider
OIF	Operation Iraqi Freedom
OEF	Operation Enduring Freedom
OMB	Office of Management and Budget
PSC	Private Security Companies
PMC	Private Military Company
PMF	Private Military Firms
SIGAR	Special Inspector General for Afghanistan Reconstruction
SIGIR	Special Inspector General for Iraq Reconstruction
SPOT	Synchronized Predeployment and Operational Tracker
TCE	Transaction Cost Economics
UCMJ	The Uniform Code of Military Justice
UN	The United Nations
US	The United States
USAID	United States Agency for International Development
USC	United States Code

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## I. INTRODUCTION

### A. DEFINITION OF PRIVATE MILITARY COMPANIES (PMC)

Some scholars define private security as any activity that is undertaken by a company to protect a “noun,” that is, an individual, a place, or a thing.<sup>1</sup> Many others make a broader definition that covers some other key services such as presenting intelligence analysis, operational coordination, and training of security forces or law enforcement personnel.<sup>2</sup> The National Defense Authorization Act for Fiscal Year 2008 (P.L. 110-181 Sec. 864) describes private security as functions associated with protecting individuals, facilities, or properties, and any other activity for which contractors are obliged to carry weapons. However, such a definition excludes unarmed personnel who are performing functions directly related to security.<sup>3</sup>

International law is rife with conventions that define mercenarism; nevertheless, written documents that clearly seek to define private military companies (PMCs) are scarce. The Geneva Conventions, which are the only globally accepted documents that establish norms for humanitarian treatment of victims of war in times of armed conflicts, define the term “mercenary,” which had historically played a significant role in warfare; however, do not define the term “private military company,” which is a relatively new phenomenon for international law. Although Article 47 of the Geneva Convention “deprives mercenaries of the privilege to serve as lawful combatants and the immunity to be treated as prisoners of war upon capture,”<sup>4</sup> there remains confusion about whether

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<sup>1</sup> Moshe Schwartz, “The Department of Defense’s Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress,” *CRS Report R40835*, September 29, 2009, 2.

<sup>2</sup> *Ibid.*

<sup>3</sup> *Ibid.*

<sup>4</sup> Todd S. Milliard, “Overcoming Post Colonial Myopia: A Call to Recognize and Regulate Private Military Companies,” *Master’s Thesis*, 2003, 41.

PMCs represent “a new form of mercenary activity”<sup>5</sup> or not. The United Nations International Convention Against the Recruitment, Use Financing and Training of Mercenaries, and The Convention for Elimination of Mercenarism in Africa also define mercenarism, even though these definitions are by and large reproductions of the definition that was made by the Geneva Conventions. Although both documents prohibit mercenarism, there still remain challenges regarding enforcement of existing regulations. The Montreux Document, which was signed in 2009 by seventeen countries including the United States, Afghanistan, and Iraq, is currently the most comprehensive effort to define PMCs. It is not a binding, but an advisory document that promotes best practices regarding utilization of PMCs by States. According to the Montreux Document; PMCs are;

private business entities that provide military and/or security services, irrespective of how they describe themselves. Military and security services include, in particular, armed guarding and protection of persons and objects, such as convoys, buildings and other places; maintenance and operation of weapons systems; prisoner detention; and advice to or training of local forces and security personnel.<sup>6</sup>

PMCs perform a wide variety of functions in different states and on behalf of different entities. However, in this thesis, PMCs are conceptualized as alternative service providers, which are contracted out by the United States governmental agencies to perform various functions on behalf of the United States government in contingency operations in Iraq and in Afghanistan. In this regard, any private firm that executes at least one of the tasks that are mentioned above will be considered a PMC. Therefore, the definition that the Montreux Document presents will provide the basis of this thesis.

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<sup>5</sup> Sabelo Gumedze, “Elimination of Mercenarism in Africa: A Need For a New Continental Approach,” *ISS Monograph Series*, No.147, July 2008, 21. Also see the report by United Nations Working Group on Use of Mercenaries, at: <http://www.unhchr.ch/hurricane/hurricane.nsf/0/F8B77250C05361F3C125731A004B0E6D?opendocument> (accessed August 11, 2010).

<sup>6</sup> See Montreux Document, 9, at: [http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/\\$FILE/ICRC\\_002\\_0996.pdf](http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/$FILE/ICRC_002_0996.pdf) (accessed July 19, 2010).

## **B. DIFFERENCES BETWEEN MILITARIES AND PMCS**

According to Max Weber, a state has “the monopoly on the legitimate use of physical force” within its own territory.<sup>7</sup> A state monopolizes the use of force by delegating some of its authority to the military, which has been considered by some scholars to be the only legitimate tool of a state authorized to use force if necessary. When PMCs emerged as alternative security providers, particularly after the end of the Cold War, scholars began to debate whether outsourcing security is appropriate, cost-efficient and useful, or not.<sup>8</sup>

Both militaries, which are public agencies, and PMCs, which are private corporations, are security providers; however, there are striking differences between them. The first difference is that unlike militaries, private military is not considered to be a profession. Samuel Huntington defines professionalism by means of three primary characteristics: expertise, social responsibility, and corporateness.<sup>9</sup> He conceptualizes the military as a profession, only if its officer corps has internalized all of these characteristics. According to Huntington, what separates an officer from a mercenary is that while for an officer, social responsibility outweighs monetary motivation; for a mercenary, private gain is the primary motivation. When the criteria that Huntington uses to measure professionalism are applied to PMCs, it becomes clear that private security is not a profession for two prominent reasons: first; money, most of the time even if not always, outweighs social responsibility in the private military sector. Second; unlike militaries, PMCs lack of corporateness. PMCs are private entities that have distinct organizational cultures and norms. Expertise, on the other hand, is perhaps the most

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<sup>7</sup> Max Weber, “Politics as a Vocation,” in O’Neil and Rogowski, eds., *Essential Readings of Comparative Politics* (New York: W.W. Norton & Co., 2006), 23. Also see Thomas C. Bruneau and Scott D. Tollefson, eds., *Who Guards the Guardians and How* (Texas: University of Texas Press, 2006), 18.

<sup>8</sup> Peter Warren Singer, *Corporate Warriors: The Rise of the Privatized Military Industry* (Ithaca: Cornell University Press, 2003), 49. Also see Deborah Avant, *The Market for Force: The Consequences of Privatizing Security* (New York: Cambridge University Press, 2005), 1–5.

<sup>9</sup> Samuel Huntington, *The Soldier and the State: The Theory and Politics of Civil-Military Relations* (London: Belknap/Harvard University Press, 1985), 8.

important reason that principals prefer PMCs, as they provide some services that require considerable proficiency. Nevertheless, though necessary, expertise is not sufficient alone to make private military a profession.

The second difference is that militaries are responsible to both the state and the society, whereas PMCs are only responsible to their principals in terms of their contracts. As Martha Minow states, “Military training, unit discipline, the Uniform Code of Military Justice, and international legal standards governing war and armed conflicts ensure accountability for the military but not for private corporations and their employees engaged in military work.”<sup>10</sup> According to Peter Warren Singer:

Private employees have distinctly different motivations, responsibilities, and loyalties than those in the public military. No matter their background, while in a private company, employees are directly responsible to the corporation and its executives; they are hired, fired, promoted, demoted, rewarded, and disciplined by the management of their private company, not by government officials or the public.<sup>11</sup>

There are many regulations and laws that keep militaries accountable at both national and international levels. However, there is neither overarching international regulatory framework nor effective regulatory mechanisms at the national level that keep PMCs accountable, including the Geneva Conventions. Moreover, even though some countries have written laws and regulations that seek to exert control over PMCs, enforcement still remains a challenge. Despite the patches to existing gaps in regulations, some PMC personnel still fall outside of the national and international regulatory framework. In other words, PMCs in a sense operate in the grey area.<sup>12</sup>

Last but not least; while for militaries there is only one legitimate principal (state), for PMCs, there are many options, including: states, international organizations, such as

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<sup>10</sup> Martha Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” in Jody Freeman and Martha Minow, eds., *Government by Contract* (Cambridge: Harvard University Press, 2009), 115.

<sup>11</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 154.

<sup>12</sup> Fred Schreier and Marina Caparini, “Privatizing Security: Law, Practice and Governance of Private Military and Security Companies,” *paper (Occasional Paper No: 6) presented as part of the policy dialogue on issues pertaining to the core mission of Geneva Centre for the Democratic Control of Armed Forces (DCAF) in Geneva*, March 2005, 57.

the UN, regional organizations, non-governmental organizations (NGOs), private corporations, and weak governments. Picking and choosing between multiple principles brings about many potential hazards on the part of the governments that employ them, while providing PMCs with considerable flexibilities. Unlike militaries, PMCs have the opportunity to select between these alternatives, and to switch sides, depending on who pays the most. Integrity and probity, which are important components of the military profession, do not make sense in the private military sector.

### **C. CLASSIFICATION OF PMCS**

According to Moshe Shwartz, functions performed by PMCs may basically be classified into two major types: armed services and unarmed services. Armed services include static security, convoy security, security escorts and personal security, whereas unarmed services encompass operational coordination, intelligence analysis, hostage negotiations, and security training.<sup>13</sup> However, this classification is so general that we cannot comprehend the capabilities of the individual firms that constitute the industry.

The United Kingdom “Green Paper” classifies the PMCs according to the services they provide: a) combat and operational support; b) military advice and training; c) arms procurement; d) intelligence gathering; e) security and crime investigation; and f) logistical support.<sup>14</sup> This categorization points to specialization in the Private Military Industry; however, data shows that even though specialization is an essential characteristic in the industry, some PMCs provide more than one service at a time and do not fit perfectly on this scale.

Doug Brooks provides a simpler classification, naming the industry as Military Service Providers (MSP) and dividing it into three main types: a) Nonlethal Service

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<sup>13</sup> Schwartz, “The Department of Defense’s Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress,” 2.

<sup>14</sup> UK Foreign and Commonwealth Office, “HC 577 Private Military Companies: Options for Regulation,” *A report by London Stationary Office*, February 12, 2002, 10.

Providers (NSPs); b) Private Security Companies (PSC); and c) Private Military Companies (PMC).<sup>15</sup> Then Brooks divides these main categories into subcategories.<sup>16</sup>

Peter Singer replaces the term PMCs with “Private Military Firms” (PMFs).<sup>17</sup> He believes that PMFs are organized to supply one of three basic functions: direct military support, advisory and training, or non-lethal aid and assistance. He uses the “tip of the spear” tool to place three types of PMFs along the range of three main military functions. He classifies PMFs as military provider firms, military consulting firms, and military support firms. According to Singer, military provider firms offer direct tactical military assistance to clients. Executive Outcomes (EO) is one of the prominent examples of military provider firms. Military consulting firms, on the other hand, provide “high-quality tactical, operational and strategic advice for the structuring, training, equipping and employment of armed forces.”<sup>18</sup> They largely draw on retired senior and non-commissioned officers.<sup>19</sup> For example, Military Professional Resources Inc. (MPRI), which provides military advice and training, and which is famous for its success in turning the Croat militia into a NATO-style army during “Operation Storm” in 1995, is one of the leading military consulting firms in the United States. Lastly, military support firms provide “logistics, intelligence, and maintenance services to armed forces.”<sup>20</sup> Halliburton and Kellogg, and Brown and Root, are examples of military support firms.

Deborah Avant argues that many private firms today offer distinct military functions simultaneously, and may appear in more than one specific region on the spear at a particular time; therefore, she argues, it is not useful to classify them according to their support type. She provides a different classification based on the contracts, rather

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<sup>15</sup> Doug Brooks, “Protecting People: the PMC Potential,” *a working document presented as Comments and Suggestions for the UK Green Paper on Regulating Private Military Services*, July 25, 2002, 2, at: <http://www.hoosier84.com/0725brookspmcregs.pdf> (accessed June 26, 2010).

<sup>16</sup> Doug Brooks, “Protecting People: the PMC Potential,” 2.

<sup>17</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 88–100.

<sup>18</sup> Steven Brayton, “Outsourcing War: Mercenaries and the Privatization of Peacekeeping,” *Journal of International Affairs*, Vol. 55, No. 2 (Spring 2002), 307.

<sup>19</sup> Peter Warren Singer, “Private Military Industry and Iraq: What Have We Learned and Where to Next,” *Policy Paper for DCAF* (November 2004), 3.

<sup>20</sup> Ibid.

than the firms.<sup>21</sup> Like Singer, she uses the “tip of the spear” tool to categorize contracts. She breaks down the services into two parts: police and military functions. While she classifies military functions as “armed operational support, unarmed operational support on the battlefield, unarmed military advice and training, and logistical support,” she categorizes police functions as “armed site security, unarmed site security, police advice and training, crime prevention and intelligence.”<sup>22</sup>

Nicholas Dew and Bryan Hudgens revise both Avant’s and Singer’s “tip of the spear” diagrams, and set forth a more comprehensive “tip of the spear” to represent the capabilities of the individual firms in the industry. They analyzed as many as 2,500 individual capabilities that various firms have in the private military sector that they think “is made up of quite different sub-sectors, which are probably better thought as a patchwork quilt than as elements up and down the spear.”<sup>23</sup> They classify primary capabilities of PMFs into three categories: operational capabilities, which include attack operations and protection services; advisory and training capabilities; and support service capabilities, which encompass different sub-categories ranging from tactical equipment maintenance and operation to admin services.<sup>24</sup>

For the purpose of this thesis, we will use the classification of PMFs that Dew and Hudgens presented; however, we will call them PMCs, rather than PMFs. “The tip of the spear” that they provided is not only comprehensive enough to demonstrate the capabilities of the individual firms, but also simple enough to grasp the basic functions that the sector is able to supply.

#### **D. BRIEF HISTORY OF PMCS**

Private security dates back to the beginning of civilizations. In the past, soldiers for hire have been called many names: soldiers of fortune, condotierri, free companies, freelancers, “Julius Caesar”, and “dogs of war.” Mercenaries, however, have begun to

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<sup>21</sup> Avant, *The Market for Force: The Consequences of Privatizing Security*, 17.

<sup>22</sup> Ibid.

<sup>23</sup> Nicholas Dew and Bryan Hudgens, “Evolving Private Military Sector: A Survey,” *Acquisition Research Sponsored Report Series NPS-AM-08-012*, August 11, 2008, 17.

<sup>24</sup> Ibid., 18.

gain prominence since the formation of modern nation states. Therefore, the time frame, which begins with the modern nation state and continues to the present time, is particularly important in terms of evolution of PMCs.

In a sense, the most significant factor that caused the formation of modern nation states was the cost of war. In an anarchic international system, a sufficient amount of capital and a large population were so critical that without them it was too difficult for any state to provide its citizens with security and to survive as a sovereign entity. States had no choice but to establish institutions such as taxation systems and conscription, in order to supply financial and human capital, which are required to afford their costly wars. To serve this purpose, a social contract has been established between the citizen and the modern nation state.<sup>25</sup> According to this contract, citizens would demand security from the state in return for paying regular taxes and serving as soldiers in the army when the state was at war. Whether a nation would be able to survive as a sovereign entity in the international system or not, by and large, would depend on its capability to “monopolize the use of force”<sup>26</sup> through raising soldiers, maintaining national armies, and using them to achieve their political goals. However, there were also states with insufficient population to maintain an army, but having the financial means to hire one, and predictably they have outsourced these military capabilities to materialize their political objectives. For example; on the brink of the French Revolutionary wars, half of the Prussian army consisted of soldiers from abroad who were fighting for money.<sup>27</sup> The best troops that Napoleon used against Russia were Italian mercenaries.<sup>28</sup> By the end of the Napoleonic Wars, Britain was by far the most highly taxed country in Europe.<sup>29</sup> Taxes collected in Britain at that time were roughly twice as much as those collected in France.<sup>30</sup>

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<sup>25</sup> Jean-Jacques Rousseau, *The Social Contract*, in P.D. Jimack, ed., *The Social Contract and Discourses* (Rutland, Vt: Charles E. Tuttle, 1993), 203.

<sup>26</sup> Weber, "Politics as a Vocation," 23.

<sup>27</sup> David Isenberg, "Private Military Contractors and U.S. Grand Strategy," *PRIO Report*, 2009, 18.

<sup>28</sup> Ibid.

<sup>29</sup> Ibid.

<sup>30</sup> Ibid.



Traditionally, mercenaries have played important roles in warfare in the United States. For instance; some notable American heroes, like Friedrich Wilhelm Augustus von Steuben and Tadeusz Kosciuszko, were in fact foreign officers hired to organize, train and lead the Continental Army.<sup>31</sup> During the American Civil War (1861-1865) Washington hired private companies to get strategic intelligence.<sup>32</sup> For example; Pinkerton, which was one of the prominent private detective companies, had been hired to spy on the South.<sup>33</sup> During both World War I and World War II, the U.S. has outsourced private companies. In World War II, the government of China contracted with American fighter pilots, who were also known as the Flying Tigers to fight the Japanese.<sup>34</sup> The Kellogg Company, which is the predecessor of current engineering and construction companies, has been one of the biggest contractors that supply services for the U.S. Agencies since WWII. Kellogg Company participated in the Manhattan Project, which brought the first atomic bombs into existence.<sup>35</sup> Brown and Root constructed naval stations and ships for the U.S. Navy.<sup>36</sup> Kellogg Brown & Root Company (KBR) was the prominent private company that took the lead in construction projects during the Vietnam War.<sup>37</sup> During the Gulf War, the U.S. outsourced numerous logistical and basic security functions to private companies.

## **E. THE RISE OF THE PRIVATE MILITARY INDUSTRY**

Nicholas Dew and Bryan Hudgens state that what has given rise to a boom in the sector has two dimensions: the impact of the evolution of demand-side factors, and the influences of the evolution of supply-side factors.<sup>38</sup> They note that the prominent demand

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<sup>31</sup> Jay James Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts* (Westport USA: Praeger Security International, 2008), 25.

<sup>32</sup> Ibid., 26.

<sup>33</sup> Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 26.

<sup>34</sup> Isenberg, "Private Military Contractors and U.S. Grand Strategy," 19.

<sup>35</sup> Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 27.

<sup>36</sup> Ibid.

<sup>37</sup> Ibid.

<sup>38</sup> Dew and Hudgens, "Evolving Private Military Sector: A Survey," 43.

factors that have led to a boom in the industry are failing states, rising wealth, natural resource dependencies, and normative policy paradigms.<sup>39</sup> They emphasize that failing states are

precisely the places where governments cannot guarantee the security of individuals; hence, individuals have to make their own security arrangements. NGOs, international organizations, extractive industries and some western government agencies are driven to do work in these countries for a variety of reasons and, when they get there, they have to at least supplement local security arrangements in order to bring security up to standards their employees find acceptable.<sup>40</sup>

They highlight that the United States has a large share in the industry (53 percent)<sup>41</sup> and it was with the global war on terrorism that the sector began to do more of their business with the public sector.<sup>42</sup> As widely known, private military industry entails wide spectrum of sub-sectors such as logistics outsourcing, operation and maintenance support for tactical equipment, Explosive Ordnance Disposal/De-mining and other sub-sectors including training, advisory, engineering and construction, IT/IS security services, intelligence services, base operations, and medical services. They note that on the supply side, each individual sub-sector operating in the private military industry has its own evolutionary trajectories.<sup>43</sup> No question that technology has played a key role in shaping these sub-sectors. As Dew and Hudgens observe, "... the rapid pace of recent changes in technology has probably had quite a different effect on surveillance and information gathering than it has had on advisory activities."<sup>44</sup>

Peter Warren Singer states that the rise of the private military industry is a global phenomenon. He asserts that from a global perspective, the boom in the industry is by and large associated with the end of the Cold War.<sup>45</sup> The end of the Cold War had three

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<sup>39</sup> Dew and Hudgens, "Evolving Private Military Sector: A Survey," 45–46.

<sup>40</sup> Ibid., 46.

<sup>41</sup> Ibid., 9.

<sup>42</sup> Ibid., 45.

<sup>43</sup> Ibid., 47–48.

<sup>44</sup> Ibid., 49.

<sup>45</sup> Singer, *Corporate Warriors: The Rise of the Privatized Military Industry*, 49.

significant impacts on private military industry. First, it gave states a reason to downsize their militaries.<sup>46</sup> However, this trend simultaneously rendered millions of ex-military personnel unemployed. In 1987, there were approximately 28,320,000 soldiers in the world.<sup>47</sup> By 2000, this number had already shrunk to 22,500,000, leaving some 6 million soldiers unemployed over a decade.<sup>48</sup> This army of unemployed soldiers created a demand in the market, triggering the supply side to establish formal business entities that provide goods and services very similar to that of militaries. Second, by the end of the cold war, a large number of arms stock in a wide variety including guns, tanks, and fighter jets, became available on the open market, facilitating the acquisition of required arms, vehicles, and other military means and tools by PMCs.<sup>49</sup> Third, the end of the Cold War indirectly reignited ethnic, religious and political conflicts in the Third World, formerly held in check by superpowers.<sup>50</sup> In turn, PMCs not only have turned out to be attractive job providers for unemployed soldiers, but also have undertaken significant tasks to manage conflicts in the Third World. In some cases, as in Angola and Sierra Leone, PMCs performed some tasks very similar to that of UN peacekeeping forces.<sup>51</sup>

#### **F. THE UNITED STATES' USE OF PMCS IN CONTINGENCY OPERATIONS**

From the U.S. perspective, what has given rise to the industry, particularly after 2001, is an emerging void, which stems from the mismatch between the geopolitical objectives of the U.S. and the resources provided by the public.<sup>52</sup> As Bruneau argues, “Overall U.S. Army forces, for example, were reduced 32% from 732,000 in 1990 to

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<sup>46</sup> David Isenberg, *Shadow Force: Private Security Contractors in Iraq* (Westport, Conn.: Praeger Security International: 2009), 1.

<sup>47</sup> David Isenberg, “Soldiers of Fortune Ltd: A Profile of Today’s Private Sector Mercenary Firms,” *Center for Defense Information*, 1997, 6.

<sup>48</sup> Isenberg, “Soldiers of Fortune Ltd: A Profile of Today’s Private Sector Mercenary Firms,” 6.

<sup>49</sup> Peter Warren Singer, “Corporate Warriors: The Rise of the Private Military Industry and Its Ramifications for International Security,” *International Security*, Vol. 26, No. 3 (2001/02), 186–220.

<sup>50</sup> Isenberg, *Shadow Force: Private Security Contractors in Iraq*, 1.

<sup>51</sup> Brayton, “Outsourcing War: Mercenaries and the Privatization of Peacekeeping,” 312.

<sup>52</sup> Isenberg, “Private Military Contractors and U.S. Grand Strategy,” 19.

499,301 by 2003.”<sup>53</sup> Despite this trend, the United States has defined itself as the guarantor of global stability in the new world order; however, the U.S. public has apparently been reluctant to back this grand strategy.<sup>54</sup> In this regard, it can be said that PMCs have played a key role in matching these objectives and tools. That the United States has increased its reliance on contractors particularly after the end of the Cold War can clearly be seen in Table 1.


<b>Presence of Contractor Personnel During U.S. Military Operations</b>			
<b>Conflict</b>	<b>Estimated Personnel (Thousands)</b>		<b>Estimated Ratio of Contractor to Military Personnel</b>
	<b>Contractor</b>	<b>Military</b>	
Revolutionary War	2	9	1 to 6
War of 1812	n.a.	38	n.a.
Mexican-American War	6	33	1 to 6
Civil war	200	1000	1 to 5
Spanish-American War	n.a	35	n.a
World War I	85	2000	1 to 24
World war II	734	5400	1 to 7
Korea	156	393	1 to 2.5
Vietnam	70	359	1 to 5
			<b>The End of the Cold War</b>
Gulf War	9	500	1 to 55
Balkans	20	20	1 to 1
Iraq Theater as of early 2008	190	200	1 to 1

Table 1. Presence of Contractor Personnel during U.S. Military Operations  
(After Congressional Budget Office, Contractors’ Support of U.S. Military Operations in Iraq)

<sup>53</sup> Thomas Bruneau, n.d., *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations* (the draft of a forthcoming book taken from the author), 248.

<sup>54</sup> Ibid., 5.

During the first ten years of the post-Cold War period, the Clinton administration, and especially Vice President Al Gore, believed that handing over some security work from government employees to contractors would increase productivity while reducing costs. According to a 1995 Defense Science Board report, the Pentagon should outsource all support functions except major combat missions to save up to \$12 billion yearly.<sup>55</sup>

Although the rise of the sector is in fact a post-Cold War phenomenon, 9/11 also had a great impact on the number of contractors hired to accompany military forces. In 2002, the U.S. military was drafting a new framework to put “the third wave plan” into practice by gradually increasing its long-run dependence on private military contractors. This plan had three main objectives: first, to release the military work force and its capabilities for the global war on terrorism; second, to enable commanders to concentrate on winning the war by outsourcing other supplementary functions; and third, to support the President’s Management Agenda.<sup>56</sup> During the Bush administration, reliance on PMCs increased significantly due largely to Global War on Terrorism strategy. Thus, PMCs have turned out to be an indispensable part of the contingency operations in Iraq and Afghanistan.

The Transparency and Accountability in Military and Security Contracting Act (S. 674), which was introduced by Senator Obama in February 2007 as an amendment to the 2008 Defense Authorization Act that was then referred to the Senate Armed Services Committee but never passed into law, frames the responsibilities of federal agencies that inform Congress about the numbers of PMC personnel employed, killed, and wounded, and disciplinary actions taken against them.<sup>57</sup>

In February 2009, the Obama administration brought in a number of changes and improvements associated with reducing state expenditures on the outsourcing of some critical services, such as military security and intelligence, and increasing the role of full-time government workers in such areas.<sup>58</sup> The Obama administration also promised to

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<sup>55</sup> Isenberg, “Private Military Contractors and U.S. Grand Strategy,” 19.

<sup>56</sup> Isenberg, *Shadow Force: Private Security Contractors in Iraq*, 17.

<sup>57</sup> Isenberg, “Private Military Contractors and U.S. Grand Strategy,” 15.

<sup>58</sup> Ibid.

improve the quality of the government staff that are overseeing and auditing contracting processes.<sup>59</sup> Moreover, Obama's 2010 budget notes, "The administration also will clarify what is inherently a governmental function and what is a commercial one; critical government functions will not be performed by the private sector for purely ideological reasons."<sup>60</sup>

## **G. RISKS ASSOCIATED WITH RELIANCE ON PMCS**

In his book, *Private Sector, Public Wars*, Jay James Carafano emphasizes the increasing U.S. reliance on contractors by these words:

In Vietnam, for every one hundred soldiers one contractor was employed. During the Gulf War (1991), one contractor was on the battlefield for every fifty soldiers. During OIF, contractors made up on out of every ten personnel. Only six years later, one contractor supported government operations in Iraq for about every 1.5 soldiers.<sup>61</sup>

There are many reasons that the United States relies on PMCs in contingency operations. For instance, PMCs can be quickly mobilized and demobilized, and they may free up military personnel to focus on offensive combat operations.<sup>62</sup> However, reliance on PMCs runs the risk of undermining the integrity and the effectiveness of the military for three prominent reasons: First, PMCs appropriate the human capital of militaries by offering readily trained officer corps higher salaries.<sup>63</sup> Second, advanced technology and expertise that PMCs provide keep militaries from generating their own capacities

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<sup>59</sup> Isenberg, "Private Military Contractors and U.S. Grand Strategy," 15.

<sup>60</sup> David Isenberg, "Dogs of War: Two Little Words," *United Press International*, June 13, 2008. at: [http://www.upi.com/Top\\_News/Special/2008/06/13/Dogs-of-War-Two-little-words/UPI-50001213396321/](http://www.upi.com/Top_News/Special/2008/06/13/Dogs-of-War-Two-little-words/UPI-50001213396321/) (accessed August 11, 2010).

<sup>61</sup> Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 38.

<sup>62</sup> Shwartz, "The Department of Defense's Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress," 8.

<sup>63</sup> Minow, "Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy," 124.

internally.<sup>64</sup> Third, PMCs weakens the integrity and the effectiveness of the military by employing subcontractors that the military would not normally wish to work with.<sup>65</sup>

To begin with, PMCs and militaries are in a sense rivals, since they both rely on the same human capital that performs close missions. PMCs usually specialize in a particular area. They employ personnel who have considerable expertise and experience in that area. Most of these personnel are former soldiers, who were previously trained in militaries. PMCs generally offer attractive salaries to the talented officers, who retire to begin a new career. The better-paying alternative sometimes appeals to these officers, motivating them to retire from the military earlier than they had planned. In turn, they leave the military in order to earn much more money in the private sector.

Broadly speaking, reliance on PMCs for advanced technology, and sophisticated weapon and logistics systems prevents militaries from developing their own capacities. This weakens the military strength, leaving them vulnerable to risks related to sustainability, maintenance, and control. Asymmetrically established contracts, which provide a highly specific asset under a highly unpredictable environment where management and oversight becomes difficult for the principal, are likely to put the principal into a disadvantageous position. It is likely that a PMC, which has a logistical contract with DoD, may reject to escort a logistical convoy, compensating for the extraordinary risks about the mission. It is also likely that compensating for failing to pay for its subcontractors, This PMC may leave the troops on the ground without food and other critical supplies, such as batteries and oil. In sum, PMCs may put the mission and the troops in danger, and thus undermine the integrity and effectiveness of the military.

In addition to all the foregoing, governments may lose control over their activities “under the layers of contracting and subcontracting.”<sup>66</sup> From government’s perspective, reliance on PMCs runs the risk of indirectly employing personnel who would normally not be employed, because PMCs are not restricted to employing subcontractors. For

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<sup>64</sup> Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” 124.

<sup>65</sup> Ibid.

<sup>66</sup> Ibid., 125.

example, particularly during the Bush administration, the U.S. Congress limited the number of contractors employed by the government; however, did not put any restrictions on the number of subcontractors. On the part of governmental agencies, this policy led to the prevalent implication of contracting with a major PMC for the provision of a huge service, and leaving the accomplishment of the service at the mercy of smaller one-shot PMCs, which are subcontracted by the major PMC. This policy has also enabled politicians to conceal the actual size of the government from the public.<sup>67</sup> Inadvertently, this policy has contributed to various institutional inefficiencies. Not knowing how largely they rely on PMCs, agencies miscalculated many aspects of contingency needs. Predictably, the results have often been fraud and waste. On the other hand, bearing financial concerns, major PMCs mostly subcontracted smaller PMCs that poorly performed their tasks. The subcontractors have generally been either third-country nationals, or locals, who demanded lower salaries. They were cheap; however, they were not trained as well as home-country nationals, which at least had military experience. Thus, subcontracting had many negative impacts on governmental agencies. Due to subcontracting, governmental agencies have not only lost control over PMCs, but also unintentionally turned out to be less efficient organizations.

## **H. LITERATURE REVIEW**

Scholars, who are studying PMCs, can be divided into two major camps in terms of the type of their studies. Academicians and political scientists, such as Peter Warren Singer, Deborah Avant, Fred Schreier, Marina Caparini, Thomas Bruneau, David Isenberg, Jennifer K. Elsea, Mosche Shwartz, Doug Brooks, Simons Chesterman, Chia Lehnardt, Allison Stanger, Benedict Sheehy, Jackson Nyamuya Maogoto, Virginia Newell, and James Stephenson constitute the academic camp, whereas authors who are mostly of a journalistic origin, for instance Thomas E. Ricks, Robert Young Pelton (author and filmmaker), Jeremy Scahill (journalist), James Ascroft, Tim Spicer, Tim Shorrock (author, commentator and journalist), and Steve Fainaru (correspondent and journalist), comprise the non-academic or journalistic group.

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<sup>67</sup> Minow, "Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy," 111.



On the other hand, it is possible to classify scholars from these two camps as opponents, proponents, and impartial. Impartial are mostly the academicians that write books and articles for academic circles, and prepare reports and make assessments for various state agencies and institutions. They approach PMCs in a more objective manner than opponents and proponents. They do not overemphasize either the pros or the cons of PMCs. They accept the reality of private military industry in modern warfare, but also try to focus on how to establish effective structural mechanisms to prevent their negative impacts.

Proponents believe that unless the demand that gave rise to them diminishes, reliance on PMCs will persist. According to them, “They (PMCs) are on America’s battlefields because the government, reflecting the will of the people, wants them there.”<sup>68</sup> Some see PMCs and outsourcing as a trend. Some others claim that it is not a choice but a compulsory decision to outsource some military functions to PMCs. For instance, Department of Defense (DoD) officials state that the post-Cold War budget cuts required significant logistical personnel reductions in the U.S. military and brought about a consequential increase in contractors providing logistical support.<sup>69</sup> These scholars believe that Private Security Companies are hired when conventional forces are inadequate to the mission assigned.<sup>70</sup> They emphasize that PMCs are not doing anything on their own, but performing the tasks the officials assign to them. According to them, PMCs are not mercenaries. Furthermore, proponents usually highlight the advantages of PMCs. For instance, they often claim that they are cheaper and cost-efficient.<sup>71</sup> They believe that PMCs are particularly good at specific tasks, as well as less sensitive to casualties and able to be deployed much more quickly than the national armies.<sup>72</sup> Most of these scholars often indicate the successes of the EOs, a PMC that closed itself

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<sup>68</sup> Isenberg, *Shadow Force: Private Security Contractors in Iraq*, preface xi.

<sup>69</sup> Moshe Schwartz, “Training the Military to Manage Contractors During Expeditionary Operations: Overview and Options for Congress,” *CRS Report R40057*, December 17, 2008, 1.

<sup>70</sup> David Bromwich, “Euphemism and American Violence,” *New York Review of Books*, April 3, 2008, 29.

<sup>71</sup> Singer, *Corporate Warriors, The Rise of the Privatized Military Industry*, 113.

<sup>72</sup> Brayton, “Outsourcing War: Mercenaries and the Privatization of Peacekeeping,” 322.

immediately after the South African Law prohibited its nationals from working as mercenaries,<sup>73</sup> which is praised for its achievements in managing the conflicts in Angola and Sierra Leone in the 1990s.

Opponents by and large make assessments from an ethical perspective. Their negative perspective of PMCs is largely because: “wars had a tendency to make people in the private sector rich.”<sup>74</sup> Opponents usually promote their negative impacts and disadvantages. Most of them set forth an ethical argument to support their claims. Opponents believe that “the monopoly on the use of force”<sup>75</sup> should only belong to the state itself, so they think that PMCs eradicate state legitimacy. They generally assert that PMCs are unreliable since they are primarily money-oriented.<sup>76</sup> For the same reason, they see PMCs as unethical entities<sup>77</sup> and view them as mercenaries. Opponents also claim that “PMCs perform in the grey area of international law,”<sup>78</sup> so they believe that for a contractor, it is relatively easier to abuse international laws in wartime, since they know that even if they conduct a crime, the gaps in the law will protect them. These scholars state that PMCs are not always as cheap as believed, since the indirect and the long-term costs are not taken into account in calculations.<sup>79</sup> According to opponents, the

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<sup>73</sup> Sophie Pons, “Executive Outcomes to Close on its Own Terms,” *Daily Mail and Guardian*, November 12, 1999, 1.

<sup>74</sup> Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 26.

<sup>75</sup> Max Weber, “Politics as a Vocation,” 23.

<sup>76</sup> Brayton, “Outsourcing War: Mercenaries and the Privatization of Peacekeeping,” 323.

<sup>77</sup> Gerry Cleaver, *Subcontracting military power: The privatization of security in contemporary Sub-Saharan Africa* (Netherlands: Kluwer Academic Publishers, 2000), 141.

<sup>78</sup> S. Goddard, “The Private Military Company: A Legitimate International Entity within Modern Conflict,” *Master’s Thesis*, 2001, 8.

<sup>79</sup> Jennifer K. Elsea, Moshe Schwartz, and Kennon H. Nakamura, “Private Security Contractors in Iraq: Background, Legal Status and Other Issues,” *CRS Report RL32419*, August 25, 2008, 49.

main reason that EO seemed more successful than national armies in Angola and Sierra Leone was that unlike the UN, EO was not neutral, since it took the government's side in both cases.<sup>80</sup>

While opponents state that PMCs undermine the efforts of the United States in Iraq and Afghanistan, proponents note that PMCs' day-to-day actions, which have a tactical nature, have nothing to do with damaging strategic objectives of the United States.<sup>81</sup> Furthermore, CEOs of PMCs claim that reputation is so important in the private security industry that a good image in the public eye guarantees successive contracts, whereas a bad image can completely annihilate their businesses. David Isenberg, who is one of the prominent researchers in that area and also the author of *Shadow Force: Private Security Contractors in Iraq*, states that "the low visibility and presumed low cost of private contractors appeals to those who favor a global U.S. military presence, but fear that such a strategy cannot command public support."<sup>82</sup> He believes that "by using contractors, the U.S. also shift responsibility and blame for its actions."<sup>83</sup> From the U.S. government's perspective, utilization of PMCs as a part of strategy is the natural outgrowth of the government's recent efforts to keep pace with changing demands of the operational environment by "rebalancing between the roles of private sector and the public sector play in war."<sup>84</sup>

Nihat Dumlupinar recently wrote a Naval Postgraduate School (NPS) Master's thesis about the regulation of PMCs in Iraq. In his thesis, he examines the basic problems of utilizing PMCs in contingency operations in terms of two types of states: strong states, and weak states.<sup>85</sup> As he argues "...the incentives of strong states are related to effectiveness and efficiency and political reasons. In contrast, in most cases, PMCs are

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<sup>80</sup> Pons, "Executive Outcomes to Close on its Own Terms," 1.

<sup>81</sup> Isenberg, *Shadow Force: Private Security Contractors in Iraq*, 160.

<sup>82</sup> Ibid., 5.

<sup>83</sup> Ibid.

<sup>84</sup> Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 11.

<sup>85</sup> Nihat Dumlupinar, "Regulation of Private Military Companies in Iraq," *NPS Thesis*, March 2010, 31–36.

the only option for weak states in order to survive, because they do not have sufficient public forces and it is not easy to obtain rapid foreign assistance due to political reasons.”<sup>86</sup> He claims that weak states have no control over activities of PMCs in their own territories.<sup>87</sup> Furthermore, he set forth that the extensive use of PMCs has undermined U.S. efforts in Iraq.<sup>88</sup> In this context, he uses “the principal agent theory” and “new institutionalism” to explain the regulation problems regarding PMCs.<sup>89</sup> According to Dumlupinar: “The control dimension is the only subject of old theories. Effectiveness and efficiency, which are presented as new dimensions of civil-military relations by Bruneau and Matei, are not the subject of old theories.”<sup>90</sup> He notes that the challenges in regulation are largely associated with the weaknesses of current national and international institutions.<sup>91</sup> As a practical solution, he recommends that a registration and a licensing system might be useful instruments for regulation in the national level.<sup>92</sup> He also draws attention to the necessity of an international institution that can operate as a registering entity at the international level.<sup>93</sup> Moreover, he emphasizes the relevance of a new international law to encompass PMCs.<sup>94</sup> Finally, he highlights that provider states must have the ultimate responsibility for the illegal actions of their PMCs.<sup>95</sup>

## **I. RESEARCH QUESTION**

### **1. Importance**

Utilizing PMCs to provide security and some logistics functions in support of stabilization and reconstruction efforts has increasingly become a noteworthy issue in the

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<sup>86</sup> Nihat Dumlupinar, “Regulation of Private Military Companies in Iraq,” *NPS Thesis*, March 2010, 89.

<sup>87</sup> *Ibid.*, 90.

<sup>88</sup> *Ibid.*

<sup>89</sup> *Ibid.*, 23–27.

<sup>90</sup> *Ibid.*, 89.

<sup>91</sup> *Ibid.*

<sup>92</sup> *Ibid.*, 91.

<sup>93</sup> *Ibid.*

<sup>94</sup> *Ibid.*

<sup>95</sup> *Ibid.*

United States and in many other nations and organizations, including the United Nations.<sup>96</sup> As of September 2009, there were more contractors than American troops in Afghanistan, at a ratio of 1.63 to 1.<sup>97</sup> PMCs have participated in almost all of the peacekeeping operations conducted by the United Nations between 1990 and 2005.<sup>98</sup> This growing reliance on PMCs worldwide has encouraged the private military industry to expand its area of interests, employing large numbers of personnel, and diversifying its services in many areas. Today, the United States is increasingly relying on PMCs to perform a wide variety of tasks and services, such as: protecting individuals; transporting convoys; securing forward operation bases, edifices, and other critical economic infrastructure; supplying food and laundry services; and training the local security forces in Iraq and Afghanistan.<sup>99</sup> Considering the insufficiency of the U.S. troops in both countries, PMCs, which can be seen as “force multipliers”<sup>100</sup> for the U.S. military efforts, are playing vital roles in terms of Iraq’s and Afghanistan’s stabilization and reconstruction processes. According to U.S. government officials, both the Department of State and the Department of Defense could not do without PMCs in both Iraq and Afghanistan.<sup>101</sup>

## **2. Research Question**

Since the Obama administration is planning to complete the withdrawal of U.S. troops from Iraq by 2011, while handing over responsibilities to Iraqi security forces and gradually increasing U.S. troops in Afghanistan,<sup>102</sup> it is apparent that rebuilding efforts

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<sup>96</sup> Schwartz, “The Department of Defense’s Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress,” 1.

<sup>97</sup> Moshe Schwartz, “Department of Defense Contractors in Iraq and Afghanistan: Background, Analysis,” *CRS Report R40764*, December 14, 2009, 5.

<sup>98</sup> Avant, *The Market Force: the Consequences of Privatizing Security*, 7.

<sup>99</sup> Schwartz, “The Department of Defense’s Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress,” 1.

<sup>100</sup> *Ibid.*, 5.

<sup>101</sup> Schwartz cites Nakamura, “Private Security Contractors: Possible Legislative Approaches,” *CRS Report MM70119*, Online Video DVD (archived) in “The Department of Defense’s Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress,” 5.

<sup>102</sup> Amy Belasco, “The Cost of Iraq, Afghanistan, and Other Global War on Terror Operations Since 9/11,” *CRS Report RL33110*, September 28, 2009, 5.

in both countries will likely create new business opportunities for the private military sector. Considering current security problems in both Iraq and Afghanistan, which have weak governments and poor economies, it can be said that demand for PMCs will not diminish in the following ten or fifteen years, but rather is likely to increase. Given that, the reliance on PMCs by the United States government is likely to continue, it is important for governmental agencies to learn how to work with them. In this context, the objective of this thesis is to examine the roles that PMCs play in current stabilization and reconstruction efforts, and to analyze how PMCs can become useful instruments in contingency operations if they are properly outsourced, managed, supervised, and regulated. In this regard, this thesis will primarily focus on the question of how to better utilize PMCs in contingency operations. Other questions that this thesis will seek to answer are: 1) which tasks should be given to PMCs in contingency operations? 2) how should they be monitored and managed on the ground? And, 3) how should they be regulated so that they do not undermine stabilization and reconstruction efforts?

This thesis largely rests on regular official reports of the Congressional Research Service (CRS), Government Accountability Office (GAO), Special Inspector General for Iraq Reconstruction (SIGIR), Special Inspector General for Afghanistan Reconstruction (SIGAR), Congressional Budget Office (CBO), and Office of Management and Budget (OMB). We will also use some milestone books in the area, and provide the reader with the current literature of journals and articles. This thesis aims to carry Nihat Dumlupinar's arguments one step further by focusing on how the United States, which extensively uses PMCs in Iraq and Afghanistan, can exert better control over PMCs so that stabilization and reconstruction efforts are not undermined by those companies' misconduct or non-compliance with the terms and conditions of their contracts.

## **J. OVERVIEW OF CHAPTERS**

In the second chapter, basics of outsourcing PMCs will be examined and that there are generally two fundamental factors for governmental agencies that affect make-or-buy decisions will be discussed. The first one is transaction cost economics (TCE), which seeks to explain how firms operate in the market, how transaction costs influence

make-or-buy decisions, what restricts the boundaries of firms, and what firms do to protect themselves from the potential contractual hazards. The second factor that influences make-or-buy decisions is inherently governmental functions, also called “sovereign functions” in TCE theory. Inherently governmental functions try to establish political and legal boundaries of outsourcing, framing the role of governmental agencies in fulfilling inbred responsibilities that cannot be delegated to any other entity.

In the third chapter, primary mechanisms that the United States government agencies use to control PMCs will be examined. This chapter will seek to answer the question of how the United States may use oversight mechanisms to better manage PMCs in contingency operations. Principal-agent theory, and new institutionalism will provide a basis for the theoretical framework of this chapter. It will be argued that unless effective management and oversight mechanisms are established, not only may costs increase, but also policy objectives are negatively affected, due to waste, corruption, and abuse.

In the fourth chapter, some underlying problems regarding regulating PMCs in contingency operations will be examined to better understand how the current regulatory framework exempts private military personnel from prosecution in some cases. It will be debated that PMCs may undermine stabilization and reconstruction efforts when they are not regulated properly. The main argument of this chapter is that since there is no overarching authority in the current international system, and since failed states are not capable of exerting control over private military activity, the contracting state is the only entity that can properly regulate and effectively use PMCs in contingency operations. It will be highlighted that even though there are regulations at the national level, states are either incapable or unwilling to apply sanctions for different reasons. This chapter proposes that the United States, Iraq, and Afghanistan may use the Montreux Document

The fifth chapter will recap the arguments made in the previous chapters and provide overall considerations on how governmental agencies of the United States can better outsource, monitor, manage, and regulate PMCs in contingency operations.

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## II. OUTSOURCING PRIVATE MILITARY COMPANIES

### A. BACKGROUND

In this chapter, basics of outsourcing PMCs will be examined. For governmental agencies, there are generally two fundamental factors that affect make-or-buy decisions. The first is transaction cost economics (TCE), which focuses on how transaction costs influence make-or-buy decisions, what restricts the boundaries of firms, and what firms do to protect themselves from potential contractual hazards. The second factor that influences make-or-buy decisions is inherently governmental functions, which is also called “sovereign functions” in TCE theory. Inherently governmental functions try to establish political and legal boundaries for outsourcing, framing the role of governmental agencies in fulfilling responsibilities that cannot be delegated to any other entity.

Before discussing transaction cost economics and inherently governmental functions, it is important to identify a significant distinction between two similar concepts: outsourcing, and privatization. In the literature, these two concepts are sometimes considered to be synonymous, so are used interchangeably; however, they have two distinct meanings. While outsourcing refers to a temporary business relationship in which the principal retains all ownership rights, including the ultimate responsibility over the implementation of the outsourced function, privatization points to a long-term business relationship in which the ownership belongs to the agent, as long as the agent complies with the terms and conditions of the contract.<sup>103</sup> This distinction is important, because incorrect usage of these concepts may cause misunderstandings. More importantly, the direction of accountability shifts, as each term refers to different rights and responsibilities by means of the principal-agent relationship.

According to Stan Soloway and Alan Chvotkin, outsourcing is a reflection of three primary trends, “a fundamental shift in the role and ownership of technology, nearly revolutionary change in the management of business and institutions of all kinds, and

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<sup>103</sup> Stan Soloway, and Alan Chvotkin, “Federal Contracting in Context: What Drives It, How to Improve It,” in Jody Freeman and Martha Minow, eds., *Government by Contract* (Cambridge: Harvard University Press, 2009), 195.

difficulties on the part of the government in recruiting and retaining the talent necessary for technologically driven service delivery.”<sup>104</sup> They state that outsourcing, which is the natural product of these factors, is an important tool for the government to achieve its missions. Some specialists acknowledge that when properly managed, outsourcing for some functions may lead to higher performance, increasing the efficiency of service delivery. Others deny this argument and claim that outsourcing is an intentional policy to make the government seem smaller.

With the end of the Cold War, budget cuts by the United States Congress forced the Department of Defense to economize.<sup>105</sup> Officials believed that outsourcing some support functions would save money as well as increase efficiency. A March 1996 DoD report states, “Like the best companies and organizations in the United States, DoD has embarked on a systematic and vigorous effort to reduce the cost and improve the performance of its support activities.”<sup>106</sup> Another report, “Outsourcing and Privatization,” issued by the Defense Science Board Task Force in 1996, advises DoD to outsource its support functions except ones that are inherently governmental.<sup>107</sup> In this sense, the increasing reliance on PMCs on the battlefield is an outgrowth of a strategic decision made immediately after the end of the Cold War to replace military personnel in some areas, such as logistics, food, housing and other basic life support, with PMC personnel, so that military could focus on its core missions, such as war-fighting.

This chapter will primarily focus on the role of governmental agencies in outsourcing. It will be explained how governmental agencies such as the Department of Defense, Department of State, and United States Agency for International Development

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<sup>104</sup> Soloway and Chvotkin, “Federal Contracting in Context: What Drives It and How to Improve It,” 192.

<sup>105</sup> Allison Stanger, *One Nation Under Contract* (London: Yale University Press, 2009), 86.

<sup>106</sup> Paul G. Kaminski, “Improving the Combat Edge Through Outsourcing,” *Department of Defense Report*, March 1996, 3. at: <http://www.dtic.mil/cgi-bin/GetTRDoc?AD=ADA339258&Location=U2&doc=GetTRDoc.pdf> (accessed July 16, 2010).

<sup>107</sup> See Report of the Defense Science Board Task Force on Outsourcing and Privatization, August 28, 1996, at: [http://books.google.com/books?id=sfp-j8jHkm8C&printsec=frontcover&dq=report+of+the+defense+science+board+task+force+on+outsourcing+and+privatization&source=bl&ots=4R5oZb6GOr&sig=KCnAvmvZzw2fKoMhmeRMAXdxHE&hl=en&ei=grBATNHCJoW6sQPNosCnDA&sa=X&oi=book\\_result&ct=result&resnum=5&ved=0CCIQ6AEwBA#v=onepage&q&f=false](http://books.google.com/books?id=sfp-j8jHkm8C&printsec=frontcover&dq=report+of+the+defense+science+board+task+force+on+outsourcing+and+privatization&source=bl&ots=4R5oZb6GOr&sig=KCnAvmvZzw2fKoMhmeRMAXdxHE&hl=en&ei=grBATNHCJoW6sQPNosCnDA&sa=X&oi=book_result&ct=result&resnum=5&ved=0CCIQ6AEwBA#v=onepage&q&f=false) (accessed July 16, 2010).

(USAID), which mainly produce services for public good, make decisions about outsourcing. Also discussed will be how outsourcing has exposed these governmental agencies to the same market dynamics as private corporations, pushing them to behave similarly to firms concerning decisions about outsourcing. Although governmental agencies are different from firms in many ways, TCE helps us to better understand the main dilemma of contracting from these agencies' perspectives: when it makes sense to produce a particular good or service internally, and when it makes sense to outsource it.<sup>108</sup>

## **B. TRANSACTION COST ECONOMICS (TCE)**

Economists have long sought to understand why firms exist and how markets work. Ronald Harry Coase, who is accepted as the founder of transaction cost economics, states that firms are organized to cut down on transaction costs and operate in the market, in which “the distribution of resources is organized by the price mechanism.”<sup>109</sup> Coase maintains that unlike firms, which are governed, markets work themselves, similar to organisms.<sup>110</sup> He defines the market as an institution that “exist(s) to facilitate exchange” between firms, which produce diverse goods and services for human needs.<sup>111</sup> He states that markets function “in order to reduce the cost of carrying out exchange transactions.”<sup>112</sup> In this respect, transaction costs become the prominent factor that affect “make-or buy” decisions of firms, which have to choose between two major alternatives: contracting out a particular activity, or performing it within the firm.<sup>113</sup>

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<sup>108</sup> Steven J. Kelman, “Achieving Contracting Goals and Recognizing Public Law Concerns: A Contracting Management Perspective,” in Jody Freeman and Martha Minow, eds., *Government by Contract* (Cambridge: Harvard University Press, 2009), 154.

<sup>109</sup> Ronald Harry Coase, *The Firm, The Market, and The Law*, (Chicago: University of Chicago Press, 1988), 41. Also see Kelman, “Achieving Contracting Goals and Recognizing Public Law Concerns: A Contracting Management Perspective,” 155.

<sup>110</sup> Coase, *The Firm, The Market, and The Law*, 34.

<sup>111</sup> *Ibid.*, 7.

<sup>112</sup> *Ibid.*

<sup>113</sup> J. Eric Fredland, “Outsourcing Military Force: A Transactions Cost Perspective on the Role of Military Companies,” *Defence and Peace Economics*, Vol. 15, No. 3 (June 2004), 209.

What then are transaction costs? Coase defines transaction costs as “the cost of using the price mechanism,” “the cost of carrying out a transaction by means of an exchange on the open market,” or in simplest terms, “marketing costs.”<sup>114</sup> Similar to Coase’s definition of transaction costs, Kenneth J. Arrow elucidates the concept as “the cost of running the economic system.”<sup>115</sup> Another economist, Dahlman, classifies transaction costs as “search and information costs, bargaining and decision costs, and policing and enforcement costs.”<sup>116</sup> As it is clearly understood from the definitions and classifications provided by prominent economists of the field, it is not possible to think of any economic exchange without involvement of transaction costs. For example, when a firm decides to purchase or sell a particular amount of stock, it needs to pay a commission to the stockbroker in return for making this transaction. This money is a transaction cost for the firm, so transaction cost is something that a firm must undergo if it wants to participate in the market.

Similar to firms, governmental agencies also face typical transaction costs when dealing with PMCs. These transaction costs mainly entail costs associated with accessing market information, selection, contract management, and monitoring.<sup>117</sup> Transaction costs are specific to the transaction itself, and stem from the very contractual relationship between trading partners. In this regard, thorough analysis of transaction costs is vital to determining if it is in a governmental agency’s best interest to contract with a PMC or if it is better to use in-house capacity to carry out the same function.

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<sup>114</sup> Coase, *The Firm, The Market, and The Law*, 6.

<sup>115</sup> Kenneth J. Arrow and Tibor Scitovsky, *Readings in Welfare Economics*, (Homewood, IL: R.D. Irwin, 1969), 148.

<sup>116</sup> Carl J. Dahlman, “The Problem of Externality,” *The Journal of Law and Economics*, Vol. 22, No. 1, (April 1979), 148.

<sup>117</sup> Neil J. Harris, “Contractors and the Cost of War: Research into Economic and Cost-Effectiveness Arguments,” *NPS Thesis*, December 2006, 40–50.

## **1. The Importance of TCE in Cost Efficiency Analysis**

In a typical make-or-buy decision, governmental agencies generally use the cost benefit analysis.<sup>118</sup> However, transaction costs are often ignored in these analyses. Even though transaction costs significantly increase in contingency operations, governmental agencies for the most part neglect them while making their calculations. This is largely because of the transactional complexity of the contingency contracting. Uncertainty is high, and opportunism is likely in such environments. Therefore, it is relatively difficult for governmental agencies to precisely estimate the transaction costs of contracting with a PMC to perform a particular function in contingency operations.

Unlike firms, which mainly produce economic goods and services, governmental agencies largely produce public goods and services. Conventional wisdom says that governmental agencies are less bound by cost-efficiency than are firms. However, the importance of cost-efficiency in governmental agencies has been growing. Particularly after the end of the Cold War, cost-efficiency has increasingly become a remarkable feature of the governmental agencies in the United States. Henceforth, economizing on transaction costs to increase cost-efficiency has become a significant component of organizational decision-making in governmental agencies.

In contingency operations, governmental agencies have basically two alternatives: using a military unit, or contracting with a PMC. In this context, in order to properly decide to contract out a particular function, governmental agencies need to know whether it is less expensive to use a PMC rather than a military unit or not. However, there are extraordinary difficulties in making a comparison between a PMC and a military unit.

First, pay is just one factor that determines the total costs. If governmental agencies just rely on direct or production costs in their make-or-buy decisions, they may fail to make the right decision, either by overestimating the possible benefits of outsourcing PMCs or by underestimating the actual costs of outsourcing PMCs. Governmental agencies may waste taxpayer's dollars unless transaction costs are

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<sup>118</sup> See Circular A-76, Article 5 (a) and Article 6 (f), at: <http://www.whitehouse.gov/sites/default/files/omb/assets/omb/circulars/a076.pdf> (accessed on August 30, 2010).

thoroughly analyzed. How, for example, can costs associated with training, healthcare, retirement salaries, and compensations of military personnel be incorporated into calculations and compared? How should training costs for contractors, monitoring, information and contract management costs be taken into account while making comparisons between military units and PMC alternatives? Traditional cost analysis generally ignores these transaction costs.

The second complication is that gathering detailed data with respect to PMCs and military personnel is painstaking. For instance, a March 2010 GAO report demonstrates that the Pentagon could not provide the GAO with critical data to make a comparison, since it does not have enough information regarding “the number of military personnel that would be needed to meet the contract requirements or the cost of training personnel to carry out security functions.”<sup>119</sup>

The third complication is that even though there are aggregated data with regard to money spent on PMC, it is often difficult to break down this general data into individual contracts. For example, A 2008 CBO report states: “From 2003 through 2007, U.S. agencies awarded \$85 billion in contracts for work to be principally performed in the Iraq theater, accounting for almost 20 percent of funding for operations in Iraq.”<sup>120</sup> The Department of Defense’s share in this total is almost 90 percent (\$76 billion).<sup>121</sup> According to the CBO figures, total expenditure for private security services was between \$6 billion and \$10 billion during the 2003–2007 period.<sup>122</sup> The CBO also notes that “between \$3 billion and \$4 billion of that spending was for obligations made directly by the U.S. government for private security services in Iraq.”<sup>123</sup> Though providing a general picture, these figures are not comparable, since they do not give any idea of how

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<sup>119</sup> Richard Fontaine, “Contracting in Combat Zones: Who are Our Subcontractors?” *Congressional Testimony*, June 29, 2010, 4, at: [http://www.cnas.org/files/documents/publications/CNAS%20Testimony\\_Fontaine\\_Committee%20on%20Oversight%20and%20Govt%20Reform\\_June%2029%202010.pdf](http://www.cnas.org/files/documents/publications/CNAS%20Testimony_Fontaine_Committee%20on%20Oversight%20and%20Govt%20Reform_June%2029%202010.pdf) (Accessed August 30, 2010).

<sup>120</sup> Congressional Budget Office, “Contractors’ Support of U.S. Operations in Iraq,” *CBO Report Pub.No.3053*, August 2008, 1.

<sup>121</sup> *Ibid.*, 2.

<sup>122</sup> *Ibid.*, 13.

<sup>123</sup> *Ibid.*

much the agency would spend if it performed the same tasks internally. At this point, it is useful to look at comparable figures to better understand whether PMCs are cost-effective.

What then is the cost of contractor personnel in comparison to military soldiers? Is outsourcing really cost-effective? The CBO released a cost comparison analysis of a PMC versus its military alternative in 2008.<sup>124</sup> According to the report, “the costs of a private security contract are comparable with those of a U.S. military unit performing similar functions.”<sup>125</sup> Nevertheless, “during peacetime, the private military contract would not have to be renewed, whereas the military unit would remain in the force structure.”<sup>126</sup> To put it another way, there is no savings during wartime.<sup>127</sup> The following chart presents detailed information regarding the CBO’s comparison.

Costs of a Private Security Contract and a U.S. Military Alternative						
Type of Cost	Cost of Army Infantry Units (Millions of 2008 dollars)					Blackwater's Costs (Millions of 2008 dollars)
	Deployed Units	Case 1-1.2 Units in Rotation Base		Case 2-2.0 Units in Rotation Base		
		Rotational Units	Total Cost	Rotational Units	Total Cost	
Military Personnel	21.8	24.9	46.6	41.5	63.2	
Operations	33.2	7.4	40.6	12.4	45.6	
Equipment	0.4	0.5	0.9	0.8	1.2	
Total Costs	55.4	32.8	88.2	54.6	110.1	98.5

Table 2. Cost of a Private Security Contract and a U.S. Military Alternative  
(After Congressional Budget Office, *Contractors’ Support of U.S. Operations in Iraq*)

<sup>124</sup> Congressional Budget Office, “Contractors’ Support of U.S. Operations in Iraq,” 1.

<sup>125</sup> Ibid.

<sup>126</sup> Ibid.

<sup>127</sup> Suzanne Simons, *Master of War* (New York: Harper Collins Publishers, 2009), 256.

In this analysis, CBO took three types of costs into consideration while estimating the military unit's cost: military personnel costs, operating costs, and equipment costs.<sup>128</sup> In the analysis, the military pay rates include "basic pay, subsistence and housing allowances, plus a federal tax advantage because those allowances are not taxed,"<sup>129</sup> however exclude "free health care for military families back home, and deferred benefits, such as pay and health care for those who receive military retirement benefits."<sup>130</sup> While estimating the costs associated with Blackwater employees, CBO took personnel, monitoring, contract management, equipment, and insurance costs into consideration.<sup>131</sup> Summations on both sides were then compared. Nonetheless, training costs on both sides are not incorporated into these calculations. This is partly because while staff of organizations are usually considered "assets," money spend on their training is not recognized as "asset specific."<sup>132</sup> In other words, it is assumed that the investment in training of military personnel has no value to the organization, if these personnel leave the job.<sup>133</sup> However, since human capital of PMC relies on former military personnel, who were already trained by the military in the past; calculations that exclude training costs may misrepresent the actual situation.

The chart above shows that there is not much difference between Blackwater<sup>134</sup> and an Army infantry unit in terms of operational costs. However, this comparison does not reflect the real picture, since costs may change depending on the type of function that is outsourced, the length of contract, and the conditions under which the function is performed. Moreover, it is difficult to generalize these findings, as different PMCs would have different performances. On the other hand, there are considerable reasons that make

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<sup>128</sup> Congressional Budget Office, "Contractors' Support of U.S. Operations in Iraq," 16.

<sup>129</sup> Ibid.

<sup>130</sup> Ibid.

<sup>131</sup> Ibid.

<sup>132</sup> Harris, "Contractors and the Cost of War: Research into Economic and Cost-Effectiveness Arguments," 42.

<sup>133</sup> Ibid.

<sup>134</sup> See Xe Web site at: <http://www.xeservices.com> (accessed August 22, 2010). Xe (previously Blackwater) is a PMC, founded in United States in 1997 by Erik Prince and Al Clark. Xe is extensively used by the United States in contingency operations for military training, base security, convoy security, and personnel security.



us believe that militaries are less efficient in the long-term than PMCs. Most significantly is that, unlike PMCs, militaries are idle in peacetime. From the government's perspective, the money, which is spent on weapon, equipment, and manpower in peacetime, is a lost economic output, since most of this capital is idle when not being used.<sup>135</sup> Therefore, rather than maintaining huge forces that must be paid and trained periodically, sometimes outsourcing some tasks to PMCs only when necessary may be cost-effective. For example, in 2005, CBO estimated that over a 20-year period including both peacetime and wartime, outsourcing logistical functions to PMCs would cost around \$41 billion, whereas obtaining the same logistical functions from the United States military would cost approximately \$78 billion.<sup>136</sup> This estimation clearly shows that it is profitable for the Department of Defense to outsource some logistical functions to PMCs. PMCs also perform other functions, such as security, military training and military advice. In order to figure out which functions PMCs execute more efficiently, performances of PMCs and militaries must be measured and compared on a case-by-case basis. Although it is relatively easier to measure costs associated with logistics, it is more difficult to measure costs related to functions like security, military training and advice. Alternatively, it may sometimes be costly to utilize PMCs, particularly when there is no effective oversight mechanism to keep their activities under control. Paying for duplicate services, fraud, and sustainability problems of the reconstruction projects may yield unintended consequences if PMCs are not properly managed and supervised. In fact, effective monitoring and good contract management are themselves costly, even if there is no fraud.

## **2. Size of Governmental Agencies**

From a TCE perspective, the optimal size for a particular company and the things that it buys, produces, and sells, are by and large determined by transaction costs. The critical point is reached when the cost of organizing a transaction within the firm

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<sup>135</sup> Fredland, "Outsourcing Military Force: A Transactions Cost Perspective on the Role of Military Companies," 212.

<sup>136</sup> Congressional Budget Office, "Logistics Support for Deployed Military Forces," *A CBO Report*, October 2005, 38.

becomes equal to the cost of executing it through the market.<sup>137</sup> This threshold restricts the size of firms operating in the market. According to Coase, as firms become larger, the costs of organizing a particular transaction internally may increase because the “entrepreneur fails to make the best use of the factors of production.”<sup>138</sup> Then firms try to optimize their sizes to produce the most efficient outcome by becoming larger (keeping the operation in-house) when the internal costs are less than the costs of the exchange transaction in the open market, or becoming smaller (contracting out) as internal costs surpass market costs. In other words, transaction costs determine the optimal size of firms.

On the contrary, the size of governmental agencies is determined not only by transaction costs but also by the political context. During the post-Cold War period, public pressure on United States Congress with respect to more efficient use of taxpayer dollars has played a significant role in critical decision-making pertaining to downsizing of governmental agencies. In addition, the change in perception of threat has pushed governmental agencies to downsize in the aftermath of the Cold War. The possibility of a nuclear war during the Cold War led to large and crowded governmental agencies in the United States with central decision-making structures.<sup>139</sup> However, the end of the Cold War has changed the perception of threat. As a response to the elimination of Soviet threat, the United States Congress has downsized its governmental agencies. After 9/11, United States has declared global war on terrorism and conducted contingency operations in Iraq and Afghanistan. These operations have required governmental agencies to be more adaptable, flexible, and divisible.<sup>140</sup> As a practical solution, governmental agencies have increasingly begun to rely on PMCs in contingency operations. However, this solution has not always brought about greater cost-efficiency on the part of governmental agencies.

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<sup>137</sup> Coase, *The Firm, The Market, and The Law*, 7.

<sup>138</sup> *Ibid.*, 43.

<sup>139</sup> Anita McGahan and Joel Baum, “Outsourcing War: Transaction Cost Dynamics of PMCs After the Cold War,” paper presented at the Summer Conference 2009 on Copenhagen Business School, June 17–19, 2009, 17, at: <http://www2.druid.dk/conferences/viewpaper.php?id=5334&cf=32> (accessed June 12, 2010).

<sup>140</sup> *Ibid.*, 22.

In sum, transaction cost is an important factor that determines the optimal size of government agencies; however, it is not the only factor. There is a significant difference between a governmental agency and a firm: sovereign functions. While governmental agencies are bound by a social contract that holds them responsible for performing sovereign functions, firms do not bear any responsibility in this regard. The impact of sovereign functions, or “inherently governmental functions,” on organizational decision-making about outsourcing will be examined later. Nevertheless, it is crucial to highlight that the assessment of the trade-off between keeping these functions in-house and outsourcing them is more complex than doing basic mathematical calculations. It requires measuring possible socio-political outcomes, as well as long-term benefits and losses of the decision. Moreover, training costs for contractors, which are often ignored, need to be taken into account.

### **3. Governance Structures and Outsourcing**

TCE also studies how firms adopt institutional alternatives in order to protect their interests at minimum costs.<sup>141</sup> From a TCE perspective, the governance structure or the organizational form, which is the dependent variable, is determined by three main independent variables: asset specificity, uncertainty, and frequency.<sup>142</sup> Of these independent variables, frequency is typically omitted from debates, despite its significant impact on institutional transformations, because it is assumed that no firm would integrate vertically to produce a good or service that is rarely used. Therefore, TCE presupposes that a firm would only want to integrate vertically when the transaction is frequent.

The second variable, uncertainty, is often attributed to the absence of necessary information about the future. Since no firm can foresee the contingent events with a hundred percent accuracy, contracts always include some level of uncertainty. The perception of uncertainty is for the most part contingent upon the length of the contract.

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<sup>141</sup> Howard A. Shelanski and Peter G. Klein, “Empirical Research in Transaction Cost Economics: A Review and Assessment,” *Journal of Law, economics and Organization*, Vol.11, No. 2 (October 1995), 337.

<sup>142</sup> *Ibid.*, 338.

Long contracts usually bring more uncertainty than shorter ones. As the contract's timeframe gets bigger, the likelihood of incompleteness increases accordingly. The logic here is that it is more likely that a governmental agency would be concerned about deviations from the contract or possible breaches of terms and conditions written in the contract if the contract encompasses relatively longer periods of time. Moreover, longer contracts naturally bring their own issues regarding opportunism. Unfortunately, uncertainty provides PMCs with advantages over governmental agencies. PMCs use every opportunity to increase their profit margin where monitoring is difficult. This is especially the case when states hire PMCs to execute some tasks under highly uncertain conditions, such as contingency operations.

Perhaps the most important contribution that TCE made to the literature is the third variable: asset-specificity. Williamson describes asset specificity as “durable investments that are undertaken in support of particular transactions, the opportunity cost of which investments are is much lower in best alternative uses or by alternative users should the original transaction be prematurely terminated.”<sup>143</sup> TCE asserts that if a particular transaction contains highly specific assets, the transaction cost of insourcing is likely to be smaller than that of outsourcing, so it is better for the firm to make it internally, rather than buying it. Similarly, governmental agencies must be careful about asset specificity as well. They must refrain from contracting with PMCs that provide highly specific assets, such as specialized human capital and sophisticated weapon systems. If a governmental agency contracts with a PMC that provides such kind of specific assets, it may be reliant on the provision of these assets by this PMC in the long run. In this case, the PMC can renegotiate the terms and conditions of the contract as it holds unfair and asymmetrical leverage due to this highly specific asset.

According to Williamson, governance is “the institutional framework within which the integrity of a transaction is decided.”<sup>144</sup> He sets forth that while seeking to find the best form of government structure, firms must also take two primary structural factors

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<sup>143</sup> Oliver Williamson, *The Economic Institutions of Capitalism* (New York: Free Press, 1985), 55.

<sup>144</sup> Oliver Williamson, “Transaction Cost Economics: The Governance of Contractual relations,” *Journal of Law and Economics*, Vol. 22, No. 2, (October, 1979), 235.

into account: adaptability and coordination. Adaptability refers to structural characteristics like autonomy, independence, and responsiveness; whereas, coordination connotes compliance and control. As clearly seen in the table presented below, he introduces three primary types of governance structures, each of which reflects different combinations of these structural features.

<b>Table 1</b>	<b>Governance Structures</b>		
<b>Criteria</b>	<b>Hierarchy</b>	<b>Hybrid</b>	<b>Market</b>
Adaptability	Weak	Semi-strong	Strong
Coordination	Strong	Semi-strong	Weak
Efficiency	Weak	Semi-strong	Strong
Control	Strong	Semi-strong	Weak

Table 3. Governance Structures (After Oliver E. Williamson, *Public and Private Bureaucracies: Transaction Cost Economics Perspective*)

The first structure is the market, in which prices provide strong incentives for entrepreneurs to take advantage of profit opportunities. In this structure, market dynamics shape the participants' behavior, requiring them to be opportunistic and rational, even if limitedly.<sup>145</sup> Information plays a key role in market dynamics, providing advantages in terms of adaptation. TCE asserts that market structure is the most efficient means of resource use; however, it is the worst in terms of protection of specific investments.

The second type of organizational form is the hierarchy, which is also called a “fully integrated,” or “highly centralized” organizational form. Hierarchies seek to maximize control and coordination.<sup>146</sup> Efficiency and adaptation are secondary focuses in hierarchies. It is generally assumed in TCE literature that internal production is less

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<sup>145</sup> Oliver Williamson, “Public and Private Bureaucracies: A Transaction Cost Economics Perspective,” *The Journal of Law, Economics and Organization*, Vol. 15, No. 1, (1999), 311.

<sup>146</sup> *Ibid.*, 313–314.

efficient than market transactions because internal employees have low-powered incentives to work, while employees of market organizations have generally high-powered incentives to compete. This makes market organizations more opportunistic than fully integrated organizations. TCE also posits that hierarchy is the most suitable form of structure in terms of offering protection for specific assets; however, it is less effective than markets when it comes to the best use of resources.

Between these two alternatives lays another type of governance structure: hybrid type organizations. Hybrid type of governance structure reduces disadvantages of both markets and hierarchies, incorporating a combination of coordination and adaptation to the organizational form.<sup>147</sup>

The general characteristic of organizational structure that governmental agencies in the United States adopted during the Cold War was primarily defensive in nature, due largely to the Soviet threat. The main concerns of governmental agencies at that time were control and coordination, for which cost-efficiency and adaptability could be compromised.<sup>148</sup> When the end of the Cold War terminated the Soviet threat, cost-efficiency became more and more important for governmental agencies in the United States. In turn, the United States Congress has downsized governmental agencies while outsourcing PMCs for various functions previously only performed by governmental agencies themselves. Adopting a new form of governance structure, governmental agencies in the United States had shifted from pure hierarchies to hybrid type of organizations, which seek to find the best compromise between control-coordination and adaptability-efficiency dimensions through contracting with PMCs to carry out various functions. Now, it was control and coordination that would be compromised for the sake of greater cost-efficiency and adaptation.

As a result, outsourcing has pushed governmental agencies in the United States to shift from hierarchies to hybrid form of governance structures, particularly after the end

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<sup>147</sup> Williamson, "Public and Private Bureaucracies: A Transaction Cost Economics Perspective," 313–314.

<sup>148</sup> McGahan and Baum, "Outsourcing War: Transaction Cost Dynamics of PMCs After the Cold War," 17–18.

of the Cold War. Therefore, they become more vulnerable to hazards of asset specificity and uncertainty. PMCs, which provide highly specific assets in uncertain environments, pose many challenges to governmental agencies in contingency operations. Depending on the nature of the function, governmental agencies may adopt different governance structures. Hierarchy is best in terms of implementing sovereign functions, while hybrid form of governance provides governmental agencies with considerable advantages of both cost-efficiency and control if effectively regulated. Market structure is apparently not suitable for governmental agencies, despite its obvious advantages by means of cost efficiency, because control, coordination and bureaucracy are indispensable elements of their governance structures.

#### **4. Contractual Hazards**

Inarguably, contractual hazards increase transaction costs and decrease the efficiency of organizations. In this regard, how firms shield themselves from hazards with regard to exchange relationships in the market is central to TCE.<sup>149</sup>

TCE claims that in a complex economic system, contracts are usually incomplete for two reasons: bounded rationality and opportunism.<sup>150</sup> TCE posits that in any contractual relationship, rationality of partners is restricted by limited knowledge, limited time, and limited cognitive skills. It is considered that decision-makers on both sides use their constrained knowledge, skills and resources to reach a satisfying outcome, instead of an optimal outcome. Furthermore, TCE supposes that agents are opportunist entities that have strong incentives to maximize their self-interests, adapting to changing conditions and new circumstances.

It is widely accepted that every economic relationship is based on some kind of exchange between trading partners. In this sense, TCE maintains that in any exchange, one side may seek to appropriate the rents that accumulated, using its positional, legal,

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<sup>149</sup> Shelanski and Klein, "Empirical Research in Transaction Cost Economics: A Review and Assessment," 336.

<sup>150</sup> Oliver Williamson, "The Logic of Economic Organization," in Oliver E. Williamson and Sidney G. Winter, eds., *The Nature of the Firm* (New York: Oxford University Press, 1991), 92–93.

technological, or informational advantage.<sup>151</sup> Since there are potential hazards inherent in a particular economic relationship, both sides need to take precautions to protect their core interests. Firms generally employ a variety of governance structures to maximize their profits, while defending themselves from contractual hazards, depending on the particular characteristics of the transaction.

Williamson applies TCE to public agencies, trying to explain why hierarchies are more appropriate for accomplishing sovereign tasks than markets.<sup>152</sup> He notes that states may become reliant on the professional excellence of contractors if they decide to delegate their authority by contracting out some sovereign tasks, such as “foreign affairs, the military, foreign intelligence, managing the money supply, and, possibly, the judiciary.”<sup>153</sup> He draws attention to possible contractual hazards inherent in contracting these sovereign tasks, namely asset-specificity, uncertainty, and probity hazards.<sup>154</sup>

*a. The Hazard of Asset Specificity*

The hazard of asset specificity is apparent if dependency is established asymmetrically bilateral.<sup>155</sup> If in a certain contractual relationship the agent becomes more powerful than the principal in terms of highly specific assets that provide the agent with informational, positional, or technological advantages over the principal, the hazard of asset specificity takes place. For instance, capabilities of some PMCs that operate in contingencies are highly specific assets, such as weapon systems, logistics systems, managerial systems, and well-trained human capital. Private military industry, which provides these highly asset specific goods and services, may pose serious dangers to sovereign nations relying on them, depending on the level of interaction and

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<sup>151</sup> Shelanski and Klein, “Empirical Research in Transaction Cost Economics: A Review and Assessment,” 336.

<sup>152</sup> Williamson, “Public and Private Bureaucracies: A Transaction Cost Economics Perspective,” 338–339.

<sup>153</sup> *Ibid.*, 321. Also see McGahan and Baum, “Outsourcing War: The Transaction Cost Dynamics of Private Military Companies After the Cold War,” 7.

<sup>154</sup> Williamson, “Public and Private Bureaucracies: A Transaction Cost Economics Perspective,” 321–324.

<sup>155</sup> Fredland, “Outsourcing Military Force: A Transactions Cost Perspective on the Role of Military Companies,” 211.



interdependence between PMCs and states. For example; PMCs may threaten to end the contract, using its bargaining advantage that stems from an asymmetrical contractual relationship and may leave the state vulnerable to hold-up.<sup>156</sup>

***b. The Hazard of Uncertainty***

It is widely acknowledged that uncertainty has a negative impact on firms' efficiency. Economic organizations seek to operate in a predictable environment, where uncertainty is low. Uncertainty brings about institutional myopia and shortsightedness that generally prevents firms from investing in long-term projects, affecting all basic decisions about production, consumption, purchase, leasing, and investment. In addition to these negative impacts, uncertainty also negatively influences contractual relationships, adding a kind of asymmetrical advantage for the agent and leaving the principal vulnerable to potential hazards of uncertainty. It can be said that in contractual relationships, the agent has more incentives to take advantage of uncertainty than has the principal. Particularly when the agent performs its given tasks geographically far from the principal, or in places where uncertainty is high, the principal faces the hazard of uncertainty. For example, private contractors may take advantage of the chaos in wartime. PMCs can easily exploit taxpayers' dollars in times of war, as monitoring becomes much more difficult for the government agencies through war profiteering. They can overcharge their principals and commit frauds. In this regard, uncertainty provides much more leverage for PMCs than for governmental agencies.

In TCE literature, it is generally accepted that uncertainty is one of the important factors that increases transaction costs; however, it is not the only factor. Conventional wisdom in TCE literature says that asset specificity, when taken into

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<sup>156</sup> Fredland, "Outsourcing Military Force: A Transactions Cost Perspective on the Role of Military Companies," 211.

account with uncertainty, is a significant determinant of make-or-buy decisions.<sup>157</sup> In this sense, a governmental agency would more likely keep an operation in-house when this operation reflects its core competency, when uncertainty and asset specificity become more evident, and when it becomes harder to measure the quality of the service that the contractor provides.<sup>158</sup> Otherwise, governmental agency would more likely outsource the same activity in order to economize on transaction costs.

*c. The Hazard of Probity*

Central to the hazard of probity lays a straightforward concern: will the agent perform its tasks in full capacity and in a way that the principal demands? How, for instance, can the principal be sure that the agent will not shirk by unilaterally putting an end to the contract or simply switching sides? Once the principal delegates authority to the agent, it follows that he naturally wants his agent to be loyal to his objectives and not to misuse the power that is given.

In this respect, the hazard of probity refers to the moral and legal quality of the relationship between principals and agents. Williamson defines probity as “the loyalty and the rectitude with which . . . the transaction is discharged.”<sup>159</sup> He maintains that probity requires a high level of integrity.<sup>160</sup> Philip Selznick states, “The chief virtue of integrity is fidelity to self-defining principles.”<sup>161</sup> Keeping that in mind, do PMCs respect the long-term objectives of states?

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<sup>157</sup> Oliver Williamson, “Franchise Bidding for Natural Monopolies-In General and with Respect to CATV,” *The Bell Journal of Economics*, Vol. 7, No. 1, (Spring, 1976), 73–104, Scott E. Maston, “The Organization of Production: Evidence from the Aerospace Industry,” *Journal of Law and Economics*, Vol. 27, No. 2, (October, 1984), 403–417, Shelanski and Klein, “Empirical Research in Transaction Cost Economics: A Review and Assessment,” 339, David Levy, “The Transaction Cost Approach to Vertical Integration: An Empirical Examination,” *Review of Economics and Industry*, Vol. 67, No. 2 (1985), 438–445, Kelman, “Achieving Contracting Goals and Recognizing Public Law Concerns: A Contracting Management Perspective,” 156.

<sup>158</sup> Kelman, “Achieving Contracting Goals and Recognizing Public Law Concerns: A Contracting Management Perspective,” 157.

<sup>159</sup> Williamson, “Public and Private Bureaucracies: A Transaction Cost Economics Perspective,” 322.

<sup>160</sup> *Ibid.*, 323.

<sup>161</sup> Williamson cites Philip Selznick, *The Moral Commonwealth* (Berkeley: University of California Press, 1992), 322 in “Public and Private Bureaucracies: A Transaction Cost Economics Perspective,” 323.

The answer to this question largely depends on how a particular PMC defines its mission and objectives, how detailed the contract is established, and how well the contract is supervised. Considering the dangers associated with the absence of integrity in the private military sector, is there any other mechanism that keeps PMCs from shirking? Many scholars claim that reputational considerations prevent PMCs from switching sides, committing crimes, or unilaterally putting an end to the contract. However, states have to do more than expect the sector to control itself to be sure that ultimate objectives are not damaged. Minow claims that public accountability is put in danger when actors hired by the government “are not governed by anyone but themselves.”<sup>162</sup> To better understand why PMCs should be controlled by effective oversight mechanisms, we need to remember a significant difference between a military and a PMC. Unlike militaries, private security is not considered to be a profession. Personnel who work for PMCs have not internalized all of the characteristics that are required for professionalism. As mentioned in the first chapter, social responsibility and corporateness are not common characteristics in the private military sector. Although they hold a considerable amount of expertise, this factor alone does not make private security a profession. Therefore, probity hazard is likely in contracts with PMCs, particularly during contingency operations. For this reason, PMCs must be controlled through various mechanisms to ensure that they work in harmony with foreign policy goals of governmental agencies. PMCs can be forced to accept some professional norms, but without effective monitoring and punishing systems, abuses cannot be prevented.

Thus far, TCE is highlighted to show how governmental agencies are organized and how they make decisions about outsourcing. Transaction cost economics, which mostly focuses on effectiveness and efficiency dimensions, is an important factor that must be taken into account in make-or-buy decisions. Nevertheless, it is not the only factor in terms of governmental agencies. Another important factor that has a significant impact on the decision-making processes of governmental agencies regarding outsourcing particular functions to PMCs will now be discussed, that is, “inherently

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<sup>162</sup> Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” 111.

governmental functions.” Inherently governmental functions are important because they complete the trinity by adding a “control” perspective over outsourcing.

### **C. INHERENTLY GOVERNMENTAL FUNCTIONS**

The question of which functions are inherently governmental and which functions should be executed by the private sector have long been debated in the United States, where the federal government and the private sector have cooperated to implement strategic tasks associated with U.S. foreign policy objectives. In this respect, the Department of Defense was central to these debates, since it has played a key role in federal contracting with its unique structure that blends military and private military personnel.<sup>163</sup>

The Commission on Wartime Contracting in Iraq and Afghanistan, which was established by the United States Congress in 2008, issued an interim report in June 2009. The report states that understaffing of contingency contracting workforce has resulted in hiring contractors for potentially inherently governmental functions.<sup>164</sup> According to the report:

Understaffing is one of the most critical barriers to effective contract management. The shortage of properly trained acquisition professionals is evident in all phases of the acquisition process—from requirements generation to post-award execution and contract close-out. Understaffing affects other areas as well. Leadership seeks alternative solutions, and the path of least resistance has resulted in hiring contractors to fill the staffing void. This response to understaffing puts contractors in a position to potentially perform inherently governmental actions.<sup>165</sup>

The United States even contracted out coordination of PMCs in contingency operations. In 2004, Aegis Defense Services, which is a United Kingdom-based PMC, was awarded a three-year contract, which was then renewed in 2007 for two years, to

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<sup>163</sup> John R. Luckey, Valerie Bailey Grasso, and Kate M. Manuel, “Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress,” *CRS Report R40641*, February 1, 2010, 1.

<sup>164</sup> Commission on Wartime Contracting in Iraq and Afghanistan, “At what Cost? Contingency Contracting in Iraq and Afghanistan,” *Interim Report*, June 2009, 8.

<sup>165</sup> *Ibid.*

coordinate the activities of more than fifty PMCs operating in the Iraq theatre.<sup>166</sup> Currently the staff of Aegis continues to perform interagency coordination functions in Afghanistan, as contractors of Armed Contractor Oversight Directorate (ACOD).<sup>167</sup>

The basic problem with inherently governmental functions is that there is no consensus about what those functions are. Inconsistent definitions are abundant. The literature regarding inherently governmental functions provides two primary definitions. The first is a statutory definition. The Federal Activities Inventory Reform (FAIR) Act of 1998 describes an inherently governmental function as “a function so intimately related to the public interest as to require performance by Federal Government employees.”<sup>168</sup> FAIR Act provides elaboration on the meaning of the definition, but does not list inherently governmental functions and commercial activities.<sup>169</sup> FAIR Act states that inherently governmental functions include functions that “determine, protect, and advance United States’ economic, political, territorial, property, or other interests by military or diplomatic action, civil or criminal justice proceedings,” contract management, and functions that “significantly affect the life, liberty, or property of private persons . . .”<sup>170</sup>

The second definition is a policy definition. The Office of Management and Budget (OMB) Circular A-76 similarly defines the term as “an activity that is so intimately related to the public interest as to mandate performance by government personnel.”<sup>171</sup> However, it states that outsourcing certain types of services such as “guard services, convoy and plant protection services, pass and identification services, and

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<sup>166</sup> Stanger, *One Nation Under Contract*, 100.

<sup>167</sup> Commission on Wartime Contracting in Iraq and Afghanistan, “At what Cost? Contingency Contracting in Iraq and Afghanistan,” 76.

<sup>168</sup> FAIR Act of 1998, Section 5, 2-a. [http://www.whitehouse.gov/omb/procurement\\_fairact/](http://www.whitehouse.gov/omb/procurement_fairact/). (accessed March 2, 2010).

<sup>169</sup> Luckey et al., “Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress,” 27.

<sup>170</sup> Jennifer K. Elsea, “Private Security Contractors in Iraq and Afghanistan,” *CRS Report R40991*, December 22, 2009, 14, also see FAIR Act of 1998, 5(2)(B)(i),(ii),and (iii), [http://www.whitehouse.gov/omb/procurement\\_fairact/](http://www.whitehouse.gov/omb/procurement_fairact/) (accessed March 2, 2010).

<sup>171</sup> OMB Circular A-76, Attachment 1, 1-a, <http://oam.ocs.doc.gov/docs/OMB%20Circular%20A-76%20Revised%202003.pdf>. (accessed March 2, 2010).

operation of prison or detention facilities” is not forbidden.<sup>172</sup> It lists which activities are commercial and clearly forbids contracting out inherently governmental functions.<sup>173</sup>

Federal Acquisition Regulation (FAR) incorporates the policy definition of inherently governmental functions of OMB Circular A-76. FAR neither provides elaboration on the meaning of the definition, nor defines commercial activities; however, it presents a list of inherently governmental functions.<sup>174</sup> It explicitly prohibits outsourcing inherently government functions and addresses functions closely related to inherently governmental functions.<sup>175</sup>

In June 2006, DoD amended the Defense Federal Acquisition Regulation (DFARS), which is known as the DoD implementation of the FAR, by adding an extra, and exceptional rule for PMCs. According to this amendment, private security contractors are given an authorization of using deadly force “only when necessary to execute their security mission to protect assets/persons, consistent with the mission statement contained in their contract.”<sup>176</sup> DoD thinks that combat functions are inherently governmental functions, but some security functions may be considered commercial.<sup>177</sup> DoD authorizes the combatant commander to decide whether a particular security function is commercial or not.<sup>178</sup>

Different statutes and regulations contain other definitions, but they are derivations and reproductions of the two definitions mentioned above, and are similar to those of the FAIR Act and OMB Circular.<sup>179</sup> Agencies mostly make their own

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<sup>172</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: Legal Issues,” 15.

<sup>173</sup> Luckey et al., “Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress,” 27.

<sup>174</sup> Ibid.

<sup>175</sup> Ibid.

<sup>176</sup> See “Defense Federal Acquisition Regulation Supplement; Contractor Personnel Authorized to Accompany U.S. Armed Forces (DFARS Case 2005-D013),” June 16, 2006, paragraph (b), at: <http://www.acq.osd.mil/dpap/dars/dfars/changenotice/index.htm> (accessed August 11, 2010).

<sup>177</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: Legal Issues,” 16.

<sup>178</sup> Ibid.

<sup>179</sup> Luckey et.al., “Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress,” 7.

interpretations regarding which functions are inherently governmental functions, so there is no single definition. Bruneau draws attention to the political side of the story:

By condoning a vague and ambiguous definition of what activities are inherently governmental, those agencies of the U.S. government with oversight responsibility have allowed the market, including the lobbying that is a hallmark of our political marketplace, to spread into tasks, roles and missions that were previously considered the purview of the federal government. Now that PMCs have taken on the missions that were previously inherently governmental, and developed clienteles through the use of campaign funds and lobbyists, it is extremely difficult to turn the trend around.<sup>180</sup>

Some experts propose that replacement of the term “inherently governmental functions” with another phrase such as “core functions,” “mission essential functions,” or “critical government functions” would put an end to this confusion. They believe that the “inherently governmental functions” concept is so abstract and so general that it leaves governmental agencies in limbo. Core or mission essential or critical functions, on the other hand, connote more concrete meanings, since they points to agencies’ central activities which are vital for the accomplishment of their core tasks and which could have harmful impacts on their performance, reputation or existence if not performed internally.

Maogato and Sheehy argue that when a state outsources a function that is normally inherently governmental, its “monopoly on the legitimate use of force” is fragmented.<sup>181</sup> As PMCs gradually take over responsibilities that previously only belonged to militaries, the very foundation of state is undermined. In turn, states begin to lose control over use of force piece by piece, and state responsibility is put in danger. Therefore, it is better for states not to outsource certain functions that are intimately associated with the very reason for their presence. The Montreux Document, for example, clearly states that international law prohibits contracting inherently governmental functions out, such as “supervision of prisoner-of-war camps and civilian places of

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<sup>180</sup> Bruneau, n.d. *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations*, 258.

<sup>181</sup> Jackson Nyamuya Maogato and Benedict Sheehy, “Private Military Companies and International Law: Building New Ladders of Legal Accountability and Responsibility,” *Cordozo J. of Conflict Resolution*, Vol.11, No. 9, (2009), 107.

internment.”<sup>182</sup> According to the document, states should decide which service is inherently governmental and which services are commercial, taking into consideration whether outsourcing a particular service would lead PMC to directly take part in hostilities or not.<sup>183</sup> The performance of certain functions by PMCs during the implementation of combat operations is also addressed by the Duncan Hunter National Defense Authorization Act. As Section 832 of the Act articulates:

“ . . . (1) security operations for the protection of resources (including people, information, equipment, and supplies) in uncontrolled or unpredictable high-threat environments should ordinarily be performed by members of the Armed Forces if they will be performed in highly hazardous public areas where the risks are uncertain and could reasonably be expected to require deadly force that is more likely to be initiated by personnel performing such security operations than to occur in self-defense;

(2) it should be in the sole discretion of the commander of the relevant combatant command to determine whether or not the performance by a private security contractor under a contract awarded by any Federal agency of a particular activity, a series of activities, or activities in a particular location, within a designated area of combat operations is appropriate and such a determination should not be delegated to any person who is not in the military chain of command;

(3) the Secretaries of the military departments and the Chiefs of Staff of the Armed Forces should ensure that the United States Armed Forces have appropriate numbers of trained personnel to perform the functions described in paragraph (1) without the need to rely upon private security contractors; and

(4) the regulations issued by the Secretary of Defense pursuant to section 862(a) of the National Defense Authorization Act for Fiscal Year 2008 (Public Law 110–181; 122 Stat. 254; 10 U.S.C. 2302 note) should ensure that private security contractors are not authorized to perform inherently governmental functions in an area of combat operations.<sup>184</sup>

Duncan Hunter National Defense Authorization Act clearly states that in uncontrollable and unpredictable environments, in which the use of deadly force is likely, PMCs should not perform inherently governmental functions. The Act also requires

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<sup>182</sup> See the Montreux Document, 32.

<sup>183</sup> Ibid., 33.

<sup>184</sup> See Duncan Hunter National Defense Authorization Act of 2009, Section 832. at: [http://www.dod.mil/dodgc/olc/docs/2009NDAA\\_PL110-417.pdf](http://www.dod.mil/dodgc/olc/docs/2009NDAA_PL110-417.pdf) (accessed July 21, 2010).



United States Armed Forces to adopt adequate numbers of trained personnel to execute these functions. Furthermore, as we discussed earlier, outsourcing some sovereign functions is directly associated with understaffing of the contingency contracting workforce. Therefore, there is a need to increase in-house capacities of governmental agencies both in terms of trained military personnel and by means of acquisition professionals so that inherently governmental functions are only performed by governmental agencies.

#### **D. CONCLUSION**

In this chapter, two primary factors that determine make-or-buy decisions of governmental agencies are examined. The first factor is transaction cost economics and the second factor is inherently governmental functions, which is also called as “sovereign functions” in TCE theory.

TCE shows how governmental agencies make decisions about outsourcing. It is discussed that although governmental agencies are different from firms in many ways, outsourcing has exposed governmental agencies to the same market dynamics as private corporations, pushing them to behave in a similar way to firms when it comes to deciding whether to keep the function in-house or contract it out. It is discussed that governmental agencies would more likely to keep an operation in-house when this operation reflects its core competency, when uncertainty and asset specificity become more evident, and when it becomes harder to measure the quality of the service that the contractor provides. Otherwise, governmental agencies would be more likely to outsource the same activity, to economize on transaction costs.

Inherently governmental functions, which try to establish political and legal boundaries of outsourcing, are emphasized to show that they play a key role in decision-making regarding using PMCs for certain tasks in contingency operations, restricting governmental organizations from contracting out some core or sovereign functions. It is indicated that the basic problem with inherently governmental functions is that there is no consensus about what those functions are.

TCE sets forth three types of contractual hazards: asset specificity hazard, uncertainty hazard, and probity hazard. It is argued that the private military industry, which provides highly asset-specific services, may pose serious dangers to sovereign nations relying on them, determining the level of interaction and interdependence between PMCs and states. With regard to uncertainty hazard, it is noted that PMCs have more incentives to take advantage of uncertainty than have states. When the agent performs its given tasks geographically far from the principal or in places where uncertainty is high, the principal faces the hazard of uncertainty. This chapter argued that probity hazard is likely in contracts with PMCs, since unlike militaries; private security is not considered to be a profession. For this reason, PMCs must be controlled through various mechanisms to ensure that they respect the policy objectives of the governmental agencies during contingency operations. PMCs can be forced to accept some professional norms, but without effective monitoring and punishing systems, abuses cannot be prevented.

TCE perspective also states that for government agencies, rather than maintaining huge forces, which are required to be paid and trained periodically, outsourcing some tasks to PMCs only when necessary may sometimes be cost-effective. On the other hand, it may sometimes be costly to utilize PMCs, particularly when there is no effective oversight mechanism to keep their activities under control.

This chapter also debated that in response to two structural characteristics (adaptability, and coordination) institutions adopt three different types of governance structures: hierarchy, hybrid, and market. TCE establishes that:

1. Market type of governance structure is the best in terms of adaptability; however, it is the worst by means of coordination.
2. Hierarchy is the best form in terms of coordination, but the worst by means of adaptability.
3. Hybrid type of governance structure requires small concessions in terms of both adaptability and coordination, providing the organization with some level of efficiency and control.

It is explained that hierarchies are more appropriate for accomplishing sovereign tasks than markets, partly because they are intentionally designed for coordination and partly because they focus on control. Hybrid form, on the other hand, runs the risk of poor performance in terms of effectiveness, efficiency, and control dimensions. Contractual hazards are more likely in hybrid form of organizations than are hierarchies. In this regard, it can be said that governmental agencies in the United States have shifted from hierarchies to hybrid form of organizations, as they began to rely on PMCs for some functions that are formerly thought to be an inherently governmental. Therefore, they become more vulnerable to contractual hazards.

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### **III. SUPERVISING AND MANAGING PRIVATE MILITARY COMPANIES**

#### **A. GENERAL**

This chapter will seek to answer the question of how the United States may use oversight mechanisms to manage PMCs in contingency operations. It will be discussed that unless effective contract management and oversight mechanisms are established, not only may costs increase, but also policy goals are negatively affected due to waste, corruption, and abuse.

Mostly because of urgent military needs in Iraq and Afghanistan, the U.S. Congress provided governmental agencies with considerable flexibility in terms of existing procurement procedures.<sup>185</sup> However, partly because of the dearth of the required capacity to oversee and partly because of the absence of commitment to supervise and manage contracts, finance and conduct related abuses followed.<sup>186</sup> As congressional and media sources disclosed, the Halliburton Company overcharged the U.S. government \$61 million for gasoline and \$186 million for meals that were not served.<sup>187</sup> An Army investigative report found that the absence of good contractor supervision, which promoted a tolerant environment, was the main reason behind the abuses at Abu Ghraib prison, where civilian interpreters and interrogators of CACI International and Titan Corporation committed various human rights crimes.<sup>188</sup> As Schwartz states: “Many observers believe that the fallout from Abu Ghraib and other incidents, such as the shooting of Iraqi civilians by private security contractors hired by the United States government, have hurt the credibility of the U.S. military and

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<sup>185</sup> Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” 115.

<sup>186</sup> Ibid.

<sup>187</sup> Ibid.

<sup>188</sup> Department of Defense, “Investigation of Intelligence Activities at Abu Ghraib,” *Army Investigative Report*, August 23, 2004, 52, at: <http://www.defense.gov/news/Aug2004/d20040825fay.pdf> (accessed August 10, 2010).

undermined efforts in Iraq.”<sup>189</sup> It is emphasized in Field Manual 3.100-21, “to fully integrate contractor support into the theater operational support structure, proper military oversight of contractors is imperative.”<sup>190</sup> However, what we see in Iraq and in Afghanistan is that this policy was never fully implemented.

Particularly after these high profile incidents, the media, the public, and the United States Congress have raised many issues regarding the utilization of PMCs as a part of the United States’ efforts to rebuild Iraq and Afghanistan. Some of these concerns were directly associated with whether or not commanders had enough training on how to manage PMCs on the ground. By and large, these concerns were straightforward, as commanders in the battlefield complained about the vagueness of their authority to manage personnel of PMCs properly.<sup>191</sup> For instance, it is reported that military personnel at Abu Ghraib prison neither received training about how to use contractors nor were informed about the terms of contracts.<sup>192</sup> The confusion about how to manage PMCs on the ground was partly caused by insufficient training regarding the management of contractors in the battlefield and partly by commanders’ unclear lines of authority over PMCs.

Largely due to allegations of corruption, abuse and waste of taxpayers’ dollars and sustainability problems of the reconstruction projects, the U.S. Congress established the Special Inspector General for Iraq Reconstruction (SIGIR) in 2003, and Special Inspector General for Afghanistan Reconstruction (SIGAR) in 2008.<sup>193</sup> The SIGIR, SIGAR, CRS, CBO, and GAO have all published regular audits, reports, inspections, and

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<sup>189</sup> Schwartz, “Training the Military to Manage Contractors During Expeditionary Operations: Overview and Options for Congress,” 4.

<sup>190</sup> United States Department of the Army, “Contractors on the Battlefield,” *Field Manual 3-100.21*, January 2003, 1–7. at: [http://www.aschq.army.mil/gc/files/fm3\\_100x21.pdf](http://www.aschq.army.mil/gc/files/fm3_100x21.pdf) (accessed July 10, 2010).

<sup>191</sup> Schwartz, “Training the Military to Manage Contractors During Expeditionary Operations: Overview and Options for Congress,” 3. Also see Government Accountability Office, “DoD Needs to Reexamine Its Extensive Reliance on Contractors and Continue to Improve Management and Oversight,” *GAO-08-572T*, March 11, 2008, Highlights Page.

<sup>192</sup> Ibid.

<sup>193</sup> Bruneau, n.d., *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations*, 232.

lessons-learned regarding the use of PMCs in contingency operations.<sup>194</sup> Various think tank organizations, NGOs, independent reporters, and the media have played important roles in investigations and have drawn public attention to the activities of PMCs operating in Iraq and Afghanistan.<sup>195</sup> The United States Congress legislative branch has improved domestic laws and regulations to facilitate managing PMCs in contingency operations. However, as Bruneau argues, “There remains . . . a large gap between what has been mandated by law and the structures and the personnel available to meet those mandates.”<sup>196</sup>

Keeping these existing problems in mind, this chapter will largely focus on how institutional mechanisms can help fill this large gap so that governmental agencies have higher control over PMCs to protect their interests. In this regard, this chapter mainly rests on *New Institutionalism*, which provides insight to structural mechanisms and the roles of institutions in bridging the gap between regulations and political commitment, and on *Principal Agent Theory*, which helps us better understand contractual hazards inherent in any employer-employee relationship that is asymmetrically established.

## **B. NEW INSTITUTIONALISM**

Hall and Taylor define institutions as “the formal or informal procedures, routines, norms and conventions embedded in organizational structure of the polity or political economy.”<sup>197</sup> What is important in this definition, even if it is not clearly stated, is that all institutions are human creations and are intentionally designed to fulfill a purpose.<sup>198</sup> According to Bruneau, “...the process of creating and implementing institutions is all about power, and institutional power relations therefore are a primary

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<sup>194</sup> Bruneau, n.d., *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations*, 232.

<sup>195</sup> Ibid., 233.

<sup>196</sup> Ibid.

<sup>197</sup> Thomas Bruneau, “Introduction,” in Thomas C. Bruneau and Scott D. Tollefson eds., *Who Guards the Guardians and How* (Texas: University of Texas Press, 2006), 6.

<sup>198</sup> Thomas Bruneau and Richard B. Goetze, Jr., “Ministries of Defense and Democratic Control,” in Thomas C. Bruneau and Scott D. Tollefson eds., *Who Guards the Guardians and How* (Texas: University of Texas Press, 2006), 72.

concern of New Institutionalism.”<sup>199</sup> In this sense, New Institutionalism is a useful theory that helps us better understand organizational and systemic problems regarding supervising and managing PMCs in contingency operations. It attributes the challenges of controlling PMCs in wartime to the weaknesses or wrong organization of institutional environment. To summarize, the New Institutionalism perspective suggests that institutions that are capable of regulating PMCs should be strengthened and power relations among institutional mechanisms should be rearranged in a way that provides better control over PMCs. If weaknesses stem from the absence of an institution, this institution should be created to facilitate regulation.

The rest of the chapter will largely rely on new institutionalism to highlight the importance of institutions in regulating PMCs in contingency operations. Fraud, waste and abuses by PMCs are evident where institutions are weak and where institutional mechanisms do not properly work. This is especially true for Iraq and Afghanistan. The democratic political institutions of these countries were by and large injected by the United States in the last decade. Thus, democratic institutions of Iraq and Afghanistan are relatively immature. In turn, both countries need considerable amount of time to embrace democracy and its institutional norms before properly enforcing laws and regulating PMCs. On the other hand, the United States has institutions with stronger capacity than those of Iraq and Afghanistan, so the United States could exert better control over PMCs than do Iraq and Afghanistan. However, this does not mean that there are no institutional problems in the United States. Therefore, this chapter will also address these institutional weaknesses and make recommendations on how to improve them. Now, we will turn to another theory that is useful for the purpose of this thesis.

### **C. PRINCIPAL-AGENT THEORY**

“Principal-agent theory,” or “the principal agent framework” as accepted by some scholars, originated from transaction cost economics theory. According to Peter Feaver, the agent (employee) has an incentive to hide information from its principal (employer)

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<sup>199</sup> Bruneau, “Introduction,” 7.



to increase his bargaining power.<sup>200</sup> He states that the agent often seeks to take advantage of uncertainty and information asymmetry to gain a comparative advantage over the principal.<sup>201</sup> Thus, monitoring becomes much more difficult for the principal, particularly when the agent is performing his tasks far from the principal and under uncertainty.<sup>202</sup> In this respect, the principal-agent framework provides insight to contractual relationship between governmental agencies and PMCs, especially in contingency operations that take place in highly volatile environments, in which control, coordination, and communication is relatively difficult.

Central to the principal agent theory lays a simple paradox: Once the employer (principal) delegates some of his authority to the employee (agent), how can he make sure that the agent is not shirking? Peter Feaver defines shirking as an agent's deviant behavior from the principal's functional and relational goals.<sup>203</sup>

Feaver associates functional goals with the behavior of the agent:

Is the agent doing what the principal asked?

Is the agent working in full capacity?

Is the agent competent enough to do what is asked?<sup>204</sup>

He links relational goals with critical decision-making:

Does the principal make key policy decisions?

Are these key decisions are substantive,

Does the principal adjudicate which decisions can be left to the agent, and

Does the agent refrain from any behavior that weakens principal's authority even if it obeys principal's functional orders.<sup>205</sup>

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<sup>200</sup> Peter D. Feaver, *Armed Servants: Agency, Oversight, and Civil-Military Relations*, (Cambridge: Massachussetts, 2003), 71.

<sup>201</sup> Ibid., 70–71.

<sup>202</sup> Feaver, *Armed Servants: Agency, Oversight, and Civil-Military Relations*, 69.

<sup>203</sup> Ibid., 60–61.

<sup>204</sup> Ibid., 61

<sup>205</sup> Ibid.

Feaver states that if all the answers to the questions mentioned above are yes, then the agent is working.<sup>206</sup> However, if there is at least one negative answer, this means that agent is shirking.<sup>207</sup>

There are two main dilemmas in any contractual relationship: adverse selection and moral hazard problems. Adverse selection refers to the moment of hiring and means that due to “perverse incentives for the agent to misrepresent himself,” the principal cannot completely be sure about “the true preferences and capabilities” of the agent.<sup>208</sup> The moral hazard problem, which refers to the behavior of the agent after being hired, means “the principal cannot completely observe the true behavior of the agent and so cannot be certain whether the agent is working or shirking.”<sup>209</sup> Feaver suggests two mechanisms to prevent the agent from shirking: monitoring and punishment.<sup>210</sup> Through monitoring mechanisms, such as contract incentives, screening and selection, fire alarms, institutional checks, police patrols, and revising delegation decisions, the principal may overcome his own asymmetrical information disadvantage by either increasing the pressure on the agent or creating incentives for him to reveal and share information.<sup>211</sup> Through punishing mechanisms, such as restrictive monitoring, material disincentives (current and future), military justice system, and extralegal action, the principal can ensure compliance of the agent.<sup>212</sup> As a result, considering the adverse selection and moral hazard problems inherent in any principal-agent relationship; effective monitoring systems and punishment mechanisms are essential to keep the agent under control.

The principal-agent theory is helpful, since it sets a clear framework regarding major problems that are inherent in relations between PMCs and the government. James Cockayne, who uses the principal-agent theory to explain how states may exert control

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<sup>206</sup> Feaver, *Armed Servants: Agency, Oversight, and Civil-Military Relations*, 62.

<sup>207</sup> Ibid.

<sup>208</sup> Ibid., 73.

<sup>209</sup> Ibid., 74.

<sup>210</sup> Ibid., 75–95.

<sup>211</sup> Ibid., 86.

<sup>212</sup> Ibid., 94.

over PMCs, notes that similar to shirking of militaries, PMCs use different mechanisms and strategies to evade oversight.<sup>213</sup> He claims that if the principal-agent relationship is not properly structured, states may become reliant on PMCs.<sup>214</sup> Drawing attention to the fact that PMCs may play principals against each other, he warns states about the possible dangers of utilization of PMCs in certain situations.<sup>215</sup>

Keeping these possible hazards in mind, we will turn to the nature of contractual dilemmas that influence the behaviors of both the principal and the agent. Understanding both sides' concerns is important, especially for the principal, since any solution to exert better control over the agent must address these dilemmas.

#### **D. CONTRACTUAL DILEMMAS**

When the principal-agent framework is applied to contractual relationships between PMCs and governmental agencies, it becomes clear that both sides find themselves in certain dilemmas. These concerns shape not only their own behaviors, but also each other's behaviors, and often create some tension in terms of their interests, objectives and ways of conduct.

At the core of contractual dilemmas are conflicting interests of two distinct parties with different objectives.<sup>216</sup> On the one hand, there is a public entity, which seeks to achieve its security goals while economizing on transactions costs; on the other hand, there is a private firm, which is organized to maximize its profit. As a result, these diverse interests are difficult to match, particularly if the market lacks openness and competitiveness, if the principal does not have effective oversight mechanisms to control the agent in terms of conformity, propriety, and adequacy of the services it provides, and if tasks would be performed in an uncertain environment that makes monitoring difficult.

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<sup>213</sup> James Cockayne, "Make or Buy? Principal-Agent Theory and The Regulation of Private Military Companies," in Simon Chesterman and Chia Lehnardt, eds., *From Mercenaries to Market: The Rise and Regulation of Private Military Companies* (Oxford: Oxford University Press, 2007), 210.

<sup>214</sup> *Ibid.*, 208.

<sup>215</sup> Cockayne, "Make or Buy? Principal-Agent Theory and The Regulation of Private Military Companies," 211.

<sup>216</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 151.

Optimization of these two distinct interests requires adequate and accurate data with regard to past performances of PMCs, an open and competitive market, clear contract terms and conditions, transparency and close scrutiny on activities of PMCs, eradication of their murky legal status, and efforts to eliminate disadvantages regarding uncertainty and information asymmetry. Ignorance or incompleteness of these factors favors PMCs, increasing their asymmetrical advantage and bargaining power over their principals, and contractual dilemmas become inevitable.

From the governmental agencies' perspectives, the main contractual dilemma concerns delegating authority to an entity over which the government has little control. Therefore, deciding on whether to outsource a certain function or to keep it in-house is in a sense compromising between control-coordination and efficiency-adaptation. How these distinct needs can be optimized? For example, some contracts encompass relatively long-periods of time, such as "lifetime support contracts for certain highly technical weapon systems."<sup>217</sup> Such kind of contracts may expose governmental agencies to the hazard of asset specificity, even if the contract is competitively bid. In this case the governmental agency's in-house capacity erodes in proportion with reliance on PMCs. When the contract has been repeated with the same bidder, this bidder gains a comparative advantage over its rivals, and begins to monopolize the provision of this highly specific asset. Thus, governments become more and more dependent on PMCs. Should this dependence be tolerated? Or should the government specifically clarify particular functions as inherently governmental so that governmental agencies keep them in-house no matter what the costs are?

From the PMCs' perspective, there are two dilemmas. First, should they achieve their mission as quickly as possible so that they convince their principals that they are more efficient than their rivals, or should they slow the mission down and prolong the contract so that they can increase their profit margin? This dilemma stems from the mismatch between the incentives of PMCs and the existing contracting procedures of principals that punish poor performance. Some scholars believe that PMCs often have

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<sup>217</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 155.

incentives to prolong contracts.<sup>218</sup> If this is the case, the contradiction for PMCs is that even though they seek to extend the contract, since future contracts depends on current performance, they have to achieve the goals that are asked for as quickly as possible in order to prove their efficacy to their principals. The second dilemma is more significant in contingency operations. On the one hand, they have to prove that they are reliable partners to governmental agencies and ready to face any challenge to accomplish the mission. On the other hand, PMCs have incentives to refrain from undue risks to protect their corporate assets.<sup>219</sup> While the former is necessary to win the contract, the latter is required to keep their human capital at stable levels, which is essential for the company to fulfill the requirements of the contract.

As a result, optimization of these diverse interests in contingency operations is a big challenge. Furthermore, contingencies provide PMCs with more leverage than governmental agencies. Since monitoring becomes difficult, PMCs often benefit from uncertainty to increase their profit margins. Unless this positional asymmetry is eradicated by effective oversight mechanisms, governmental agencies are doomed to face contractual hazards and their negative consequences. In this regard, the contract is the primary tool that governmental agencies can use to manage PMCs. The contract is the mandate for a PMC that prescribes what he is required to do and what he is required not to do. In this sense, a well-written contract that is flexible enough to allow governmental agencies to adapt to new circumstances but detailed enough to exert effective control over PMCs is essential for effective oversight. The rest of this chapter will examine the existing contracting system in the United States. Scholars often argue that existing contracting system does not answer to the contingency needs. The argument is that while contracting in contingency operations requires quick response and flexibility but at the same time greater control, the existing system largely focuses on efficiency. Nevertheless, in contingency operations, rapid delivery of a good or service may sometimes be more crucial than cost-efficiency. In this regard, it is essential to adapt the existing system in accordance with the requirements of contingency contracting.

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<sup>218</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 157.

<sup>219</sup> *Ibid.*, 157.

## **E. CONTRACTING SYSTEM IN THE UNITED STATES**

The United States Code (U.S.C.), Federal Acquisition Regulation (FAR), the Defense Federal Acquisition Regulation Supplement (DFARS), Department of Defense 5000 series of acquisition guidance, Department of Defense Regulation 7000.14-R, the Department of Defense Financial Management Regulation, and Operational Contracting in Joint Operations (Joint Publication 4-10) establish a framework for the contracting system.<sup>220</sup> These documents clearly maintain that contracting is a continuous process that encompasses the contracting cycle as a whole, from contract award to contract closeout. Basically, federal procurement laws that regulate contracting procedures require that governmental agencies be neutral and fair to all parties.<sup>221</sup> Therefore, it is necessary that governmental agencies be responsible to pursue open and transparent contracting processes. In this regard, there are two dimensions of insuring impartiality: maintaining accountability through contracting procedures, and maintaining accountability through oversight.<sup>222</sup>

In order to maintain accountability through contracting procedures, there are national regulations in the United States that ensure accountability, transparency and neutrality. For instance, FAR obligates contracting officers to disseminate information regarding every contract that is expected to exceed \$25,000 so that any qualified firm has the opportunity to participate in the bidding.<sup>223</sup> Moreover, FAR requires Contracting Officers to disseminate basic information via the Internet, such as the type and value of the contract and the identity of the winner, for contracts awarded in excess of \$25,000.<sup>224</sup> In addition, the Code of Federal Regulation obligates PMCs that seek to work for United States government, to meet basic requirements, such as registering in the Central

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<sup>220</sup> United States Department of Defense Office of Inspector General, "Contingency Contracting: A Framework for Reform," May 14, 2010, 1, at: <http://www.dodig.mil/Audit/reports/fy10/10-059.pdf> (accessed July 20, 2010).

<sup>221</sup> Soloway and Chvotkin, "Federal Contracting in Context: What Drives It, How to Improve It," 199.

<sup>222</sup> Ibid.

<sup>223</sup> Ibid., 200. Also see 48 Code of Federal Regulations, (2009), 95, at: <http://frwebgate3.access.gpo.gov/cgi-bin/PDFgate.cgi?WAISdocID=UZPIFJ/2/2/0&WAISaction=retrieve> (accessed July 18, 2010).

<sup>224</sup> Ibid.

Contractor Registration database, in order to ensure that bidders are “legitimate entities with a business bank account, federal tax identification number, and a business address.”<sup>225</sup>

The United States maintains accountability through various federal laws, regulations and oversight mechanisms. For example, the Federal Acquisition Regulation requires PMCs to be responsible for performing their work in line with the terms and conditions of the contract, obligating the contracting entity to have the main responsibility to supervise contracts.<sup>226</sup> Contracting officers (CO) and contracting officer representatives (COR) are assigned to ensure that PMCs are performing their tasks in accordance with the terms and conditions of their contracts. Some social mechanisms also maintain accountability through oversight. For instance, other entities that share the same area of responsibility, such as local people, local security forces, media, NGOs, and other private or formal organizations, have social responsibilities to monitor and report fraud, waste and abuse by PMCs. This is generally called as “fire alarming system.” Furthermore, various institutional oversight mechanisms such as CRS, GAO, OMB, the Army Audit Agency (AAA), Defense Contract Audit Agency (DCAA), SIGIR and SIGAR, have significant roles in informing the United States Congress, government and public in general, and keeping PMCs accountable.

The United States has been working on a new contingency contracting system, incorporating the basics of the existing system, which is primarily ordered by FAR. However, beginning with the global war on terrorism, contracting professionals, scholars, and government officials have debated that the current contracting system is not suitable for contingency contracting, in which quick response is sometimes more important than cost-efficiency.<sup>227</sup> In response to changing requirements, the Joint Contingency Contracting Policy Workgroup issued a joint handbook on contingency contracting in

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<sup>225</sup> Soloway and Chvotkin, “Federal Contracting in Context: What Drives It, How to Improve It,” 200.

<sup>226</sup> Ibid.

<sup>227</sup> Commission on Army Acquisition and Program Management in Expeditionary Operations, “Urgent Reform Required: Army Expeditionary Contracting,” *The Commission Report also known as The Gansler Report*, October 31, 2007, 39, at: [http://www.army.mil/docs/gansler\\_commission\\_report\\_final\\_071031.pdf](http://www.army.mil/docs/gansler_commission_report_final_071031.pdf) (accessed July 25, 2010).

2008, adapting the contracting requirements of FAR, DFARS and Joint Publication 4-10 into contingency operations. According to the handbook, the contract monitoring system in contingency operations is basically comprised of two components: CO, and COR.<sup>228</sup> Commanders also have the responsibility to coordinate and monitor the efforts of other units, organizations, and private entities in a certain area of responsibility; therefore, it is meaningful to incorporate them into the monitoring system as an integral part.

### **1. Contracting Officer**

The CO is the only person who is authorized to control and manage all aspects of contract implementation. No other person or official, even if he is the head of a governmental agency, COR, or a military commander, is allowed to direct the execution of a contract without the clear approval of the COs.<sup>229</sup> COs utilize various tools and techniques to make sure that PMCs are executing their missions in accordance with the requirements of the contract. These tools include “contract deliverables, program reviews, and payment approvals.”<sup>230</sup> COs also use a variety of managerial instruments to take corrective action when a PMC fails to fulfill the requirements of the contract.<sup>231</sup> For example, federal regulation authorizes the contracting officer to decide the award of an option period.<sup>232</sup> The government also has the authority to delay or prohibit a PMC from “doing future business with the federal government, hold the contractor responsible for the failure to perform, and charge the contractor for any additional costs of reperformance.”<sup>233</sup>

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<sup>228</sup> Joint Contingency Contracting Policy Workgroup, “Contingency Contracting: A Joint Handbook for the 21 st Century,” *a Defense Procurement and Acquisition Policy and Strategic Sourcing Department Handbook*, December 2008, 239, at: <http://www.acq.osd.mil/dpap/pacc/cc/jcchb/Contingency%20Model/JCC/JCC%20Tools%20CD/Ch6BO.pdf> (accessed July 22, 2010).

<sup>229</sup> Ibid.

<sup>230</sup> Ibid., 201.

<sup>231</sup> Ibid.

<sup>232</sup> Ibid.

<sup>233</sup> Soloway and Chvotkin, “Federal Contracting in Context: What Drives It, How to Improve It,” 201.



## **2. Contracting Officer's Representative**

During contingency operations, contracting surveillance by contracting officers becomes harder because of continuing military operations and threats associated with local instabilities. In this regard, CORs play key roles in contract monitoring and are “the last tactical mile” of contingency contract monitoring.<sup>234</sup> In this sense, CORs constitute a bridge between COs and PMCs. CORs are responsible for monitoring PMCs and notifying COs about their performances. Nevertheless, they have no authority to make any changes that influence price, time, quality, and quantity of the delivery on the terms and conditions of the contract.<sup>235</sup> They perform regular and irregular inspections and submit performance reports to COs. According to DFARS Subpart 201.6, a COR must be a qualified, experienced and trained government employee. Furthermore, the Office of Management and Budget memorandum, which was released in November 2007, requires that all CORs appointed to a contract must be certified.<sup>236</sup> The memorandum states that after getting core training and assignment-specific training, CORs qualify to have a certificate; however, they are expected to maintain their knowledge and skills through continuous learning.<sup>237</sup>

## **3. Military Commanders**

Commanders are also responsible to ensure that all sub-units that share the same area of responsibility are working in tandem. Different field manuals and documents mention these responsibilities. For instance, the Field Manual on Counterinsurgency, which was published in 2006, highlights the significant role that contractors play in counterinsurgency operations and states that “at a minimum, commanders should know which companies are present in their [area of operation] AO, . . . commanders should

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<sup>234</sup> Commission on Army Acquisition and Program Management in Expeditionary Operations, “Urgent Reform Required: Army Expeditionary Contracting,” 43.

<sup>235</sup> United States Department of Defense Office of Inspector General, “Contingency Contracting: A Framework for Reform,” 13.

<sup>236</sup> The Office of Management and Budget, “The Federal Acquisition Certification for Contracting Officer Technical Representatives,” *OMB Report*, November 26, 2007, 2, at: <http://www.whitehouse.gov/omb/procurement/memo/fac-cotr.pdf> (accessed July 23, 2010).

<sup>237</sup> Ibid.

identify contractors operating in their AO and determine the nature of their contract, existing accountability mechanism, and appropriate coordination relationships.”<sup>238</sup> Similarly, Richard Fontaine testifies that an officer in the battlefield should at least know “how many contractors are in a particular battle space, who and where they are, and what they are doing; how their responsibilities mesh with the authorities and responsibilities of American government personnel; and how operational plans incorporate contractors into the array of forces in play.”<sup>239</sup> Nevertheless, it is difficult for commanders to fulfill these responsibilities, because although they use the same area of responsibility, PMCs operate out of their own command structure.

## **F. INSTITUTIONAL PROBLEMS IN THE UNITED STATES**

There are mainly six institutional problems that make supervising PMCs harder. The first institutional challenge is associated with doctrinal void and institutional misunderstanding of the roles that PMCs play in contingency operations. The hanging of four armed contractors working for Blackwater (now Xe) on a bridge in Fallujah in 2004 taught us that Iraqi insurgents did not see much difference between PMC personnel and U.S. military personnel. We came to realize that PMCs play such significant roles in Iraq and Afghanistan that unless managed and monitored properly, they may inadvertently undermine the United States’ efforts. Current doctrine, however, does not perfectly reflect this insight. For example, according to Singer, the fundamental problem with monitoring is the absence of a doctrine on how to manage PMCs and how to effectively integrate them to the operational plans.<sup>240</sup> Abu Ghraib and Nassir Square incidents are in a sense reflections of this institutional misconception. Another example of the absence of a coherent doctrine is that United States even contracted out the coordination of PMCs in contingency operations. In 2004, Aegis Defense Services, which is a United Kingdom-based PMC, was awarded a three-year contract, which was then renewed in 2007 for two years, to coordinate the activities of more than fifty PMCs operating in the Iraq

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<sup>238</sup> See Field Manual 3-24, *Counterinsurgency*, 2–4, 2–8, at: <http://www.fas.org/irp/doddir/army/fm3-24.pdf> (accessed July 12, 2010).

<sup>239</sup> Fontaine, “Contracting in Combat Zones: Who are Our Subcontractors?” 5.

<sup>240</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 153.

theatre.<sup>241</sup> Secretary of Defense Robert Gates articulates the absence of a comprehensive doctrine regarding the utilization of PMCs in contingency operations with those words:

without any supervision or without any coherent strategy on how we were going to do it and without conscious decisions about what we will allow contractors to do and what we won't allow contractors to do . . . We have not thought holistically or coherently about our use of contractors, particularly when it comes to combat environments or combat training.<sup>242</sup>

Thus, it becomes clear that there is an urgent need for institutional realization of the importance of supervision with respect to activities of PMCs in contingency operations. Moreover, in a contingency operation, it is important that all governmental agencies speak the same language. Establishing a doctrine that outlines clear principles and guidelines on how to manage and supervise PMCs and that reflects organizational understanding of the roles that PMCs play in contingency operations is essential for the success of the contingency missions.

The second institutional challenge is the weaknesses of interagency coordination mechanisms in contingency operations. According to Martha Minow, there is a significant institutional lacuna that provides PMCs with asymmetrical advantage. She states that, "Proceeding with their own agendas, under their own leaders, contractors may literally collide with military initiatives, and no coherent coordination of information and personnel yet exists to bridge the contractor-military divide."<sup>243</sup> In order to coordinate the operations of PMCs in Iraq, Armed Contractor Oversight Division (ACOD) was established in 2007. In February 2009, the United States established another ACOD in Afghanistan. However, there are ongoing coordination problems, particularly in Afghanistan. While ACOD in Iraq is relatively an older organization that is led and staffed by DoD personnel, ACOD in Afghanistan is a pretty new organization that is

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<sup>241</sup> Stanger, *One Nation Under Contract*, 100.

<sup>242</sup> Schwartz quotes the testimony of Secretary of Defense Robert Gates in "Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis," *CRS Report*, July 2, 2010, 15.

<sup>243</sup> Minow, "Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy," 121.

mainly staffed by Aegis contractor personnel.<sup>244</sup> Furthermore, the Memorandum of Agreement, which was signed in 2007 between the Department of Defense and Department of State to coordinate efforts to monitor PMCs, applies only to Iraq.<sup>245</sup> There is no such agreement in Afghanistan between these two governmental agencies.<sup>246</sup>

What makes oversight even much more difficult in contingency operations is the shortage of CO and CORs. Even though the reliance on PMCs has increased over the last decade, the number of COs and CORs has stayed constant; causing shortages that had many unintended consequences on contingency contracts. First, inadequacy of contracting officials pushes governmental agencies to award a huge contract to one primary PMC at a time.<sup>247</sup> Generally, this primary PMC subcontracts other PMCs to fulfill the given function. Breaking the contract into pieces and contracting out each piece to other agents, the primary PMC indirectly becomes the monitoring mechanism of the governmental agency. For example, it is reported that of about sixty known PMCs that operate in the Iraq theatre, only eight directly work for the Department of Defense, whereas the rest of them are subcontractors.<sup>248</sup> This means that the Department of Defense, which contracts out one large PMC, inadvertently loses control over subcontractors, because subcontractors are not accountable to the DoD, but to the primary PMC that employs them. If there were enough procurement personnel, contracts with PMCs would be more easily managed and monitored, because rather than subcontracting, a huge contract would be divided into smaller contracts, each supervised by at least one contracting personnel.<sup>249</sup> In addition to loss of control, subcontracting also increases the likelihood of fraud and creates inefficiencies on the governmental agencies' side. Since governmental agencies have no control over the subcontracting procedure, they sometimes circuitously employ a PMC that they would never employ otherwise. Another

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<sup>244</sup> Commission on Wartime Contracting in Iraq and Afghanistan, "At what Cost? Contingency Contracting in Iraq and Afghanistan," *Interim Report*, June 2009, 76.

<sup>245</sup> *Ibid.*, 64.

<sup>246</sup> *Ibid.*

<sup>247</sup> *Ibid.*

<sup>248</sup> Stanger, *One Nation Under Contract*, 104.

<sup>249</sup> *Ibid.*, 91.

complication is that CORs have not been properly assigned to monitor PMCs. A report by the Commission on Wartime Contracting indicates that in both Iraq and Afghanistan, some of the security CORs had no technical expertise in security.<sup>250</sup> The report reveals that one security COR in Iraq was a combat medic; another security COR in Afghanistan was field artillery.<sup>251</sup> Normally CORs are appointed by COs to oversee a number of contracts; however, under contingency operations, CORs usually perform their monitoring missions in addition to their original job responsibilities.<sup>252</sup> A report by the Commission on Wartime Contracting in Iraq and Afghanistan reveals that CORs do not have sufficient time to supervise their contracts and that they have no motivation to achieve their monitoring mission with high performance, since performance assessment criteria are based on their primary job responsibilities.<sup>253</sup> According to the report, due to the insufficiency of acquisition personnel on the ground, CORs are so overloaded with work that they cannot monitor their contracts properly.<sup>254</sup> Interviews that Commission on Warfare Contracting conducted in Afghanistan reveal that in April 2009, one of the certified CORs of the Combined Joint Task Force-101 was assigned to monitor fifteen contracts simultaneously.<sup>255</sup> According to the Commission's figures, CORs in the Afghanistan theatre are responsible for 3.55 contracts on average.<sup>256</sup>

The fourth institutional complication is that governmental agencies rarely train contracting personnel on how to supervise PMCs and do not normally appoint their best employees to oversee contracts.<sup>257</sup> The Gansler Report, which was released by the Commission on Army Acquisition and Program Management in Expeditionary Operations in 2007, revealed that contracting officer representatives, who are responsible

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<sup>250</sup> Commission on Wartime Contracting in Iraq and Afghanistan, "At what Cost? Contingency Contracting in Iraq and Afghanistan," 70–71.

<sup>251</sup> Ibid.

<sup>252</sup> Ibid., 9.

<sup>253</sup> Ibid.

<sup>254</sup> Ibid., 11.

<sup>255</sup> Ibid.

<sup>256</sup> Ibid.

<sup>257</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 154.

for managing PMCs in contingency operations, have no previous background, interaction or experience with contractors and have received little training on managing PMCs on the ground.<sup>258</sup> It has been articulated by GAO, CRS, the Commission on Wartime Contracting in Iraq and Afghanistan many times that the government must ensure that professionals in the field of acquisition management and contract administration are thoroughly trained and properly authorized to manage the challenges of modern contracting procedures.<sup>259</sup>

Fifth, contingency contracts with PMCs usually involve unclear requirements.<sup>260</sup> According to Singer: “. . . contract terms with PMFs are often unspecific, lacking outside standards of achievement and established measures of effectiveness. This leaves the principal/client at the mercy of the agent to tell him how well the contract is going and what should be done next.”<sup>261</sup> In this respect, contracting management is perhaps the most important tool to control PMCs. As Bruneau states, “The contract is the vehicle and guidance for everything contractors are paid to do. Effectiveness is only as good as the contract and the organizational processes used to plan, award, and administer the contract.”<sup>262</sup> In contingency operations, however, writing a contract with enough clarity to facilitate monitoring and management of the activities of PMCs while providing the governmental agency with sufficient flexibility to adapt to new circumstances is a considerable challenge for COs.

The last institutional problem concerns managing PMCs on the ground. As the number of contractors has increased over the last two decades, military commanders and soldiers on the ground have increasingly begun to cooperate and interact with PMCs. Aligning PMCs with the military has posed new challenges on control and command in

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<sup>258</sup> Commission on Army Acquisition and Program Management in Expeditionary Operations, “Urgent Reform Required: Army Expeditionary Contracting,” 43.

<sup>259</sup> Soloway and Chvotkin, “Federal Contracting in Context: What Drives It, How to Improve It,” 193.

<sup>260</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 154.

<sup>261</sup> *Ibid.*, 153.

<sup>262</sup> Bruneau, n.d., *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations*, 248.

the battlefield. A report issued by the CRS in 2008 expresses that a number of military commanders and service members lacked “adequate information regarding the extent of contractor support in Iraq” and “did not receive enough pre-deployment training about managing contractors.”<sup>263</sup> In this regard, managing PMCs necessitates well-trained military officers that have critical knowledge and skills regarding PMCs.

## **G. STEPS TO IMPROVE OVERSIGHT AND MANAGEMENT**

### **1. Developing a Comprehensive Doctrine**

Doctrines are written to codify general principles. They reflect institutional insight about a particular issue. Institutions use doctrines as tools to provide their members with their institutional perspective on a specific subject. However, at the center of any institution are human. Doctrines do very little unless members of institutions embrace and apply these doctrines into their daily tasks. In this sense, the presence of a well-written doctrine is not sufficient for better institutional understanding, and does not guarantee higher performance. Therefore, the challenge for institutions is to write a living doctrine that answers to the needs of their members.

The Gansler report states that an urgent need is required to develop a comprehensive doctrine that incorporates true understanding of the roles that contractors play in contingency operations in the military culture.<sup>264</sup> Unquestionably, this new doctrine should answer to the needs of contingency operations.<sup>265</sup> First, it should address the problems associated with inherently governmental functions. In this context, new doctrine should put an end to confusion about the definition of inherently governmental functions, clarifying which functions are inherently governmental, which functions are

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<sup>263</sup> Schwartz, “Training the Military to Manage Contractors During Expeditionary Operations: Overview and Options for Congress,” 3.

<sup>264</sup> Commission on Army Acquisition and Program Management in Expeditionary Operations, “Urgent Reform Required: Army Expeditionary Contracting,” 9. Also see Schwartz, “Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis,” 17.

<sup>265</sup> Schwartz, “Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis,” 17.

related to inherently governmental, and which functions are commercial.<sup>266</sup> Second, it should also establish a comprehensive framework for contingency contracting procedures that are required to respond to current contingency demands: simplified but effective procedures, clear requirements and specific standards that can easily be measured, clear lines of authorities, and larger number of professional COs and CORs. Last, it should incorporate PMCs into military operations in contingency operations, clarifying their position in the larger military command structure.

In this sense, the United States has been working on establishing a new doctrine that tries to incorporate PMCs into military operations since 2007. For instance, in 2008, the Chairman of the Joint Chiefs of Staff issued Joint Publication 4-10 Operational Contract Support, which provides a doctrine for contractor management and support during contingency operations.<sup>267</sup> In 2009, Deputy Secretary of Defense William J. Lynn released a detailed directive that points to specific responsibilities within the Department of Defense regarding contract management, contract oversight, managing contractors in the battlefield, developing policy, providing guidance, and incorporating contractors into contingency operations.<sup>268</sup> In July 2009, the Department of Defense published an instruction setting rules, policies and procedures for managing PMCs during contingency operations.<sup>269</sup> Following the instruction released by DoD, a task force on wartime contracting was established under Secretary Ashton Carter.<sup>270</sup> The task force is comprised of members from the Joint Contracting Command, Joint Staff, military services, and the Office of the Secretary of Defense.<sup>271</sup> The Department of Defense assigned an oversight mission to the task force. The task force is now establishing what the proper roles are that contractors may play in contingency operations.<sup>272</sup> According to

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<sup>266</sup> Luckey et.al., “Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress,” 1–2.

<sup>267</sup> Schwartz, “Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis,” 19.

<sup>268</sup> Ibid.

<sup>269</sup> Ibid.

<sup>270</sup> Ibid., 20.

<sup>271</sup> Ibid.

<sup>272</sup> Ibid.



the Department of Defense, findings of the task force will not only reshape the existing doctrine, but also help officials to determine which roles can be assigned to them and what should be the actual size of contractor workforce in contingency operations.<sup>273</sup> In order to provide commanders, CCOs and CORs with vital information regarding contingency contracting, Department of Defense Office of Inspector General published a report in May 2010. DoD officials state that many doctrinal changes are still underway.<sup>274</sup> They assert that incorporating PMCs into military culture requires diligence and patience.<sup>275</sup> DoD estimates that it may take three years to update the current policies, integrate PMCs into military operations, and complete training.<sup>276</sup>

## **2. Creating an Institutional Memory**

In order to decide whether PMCs are properly monitored, credible and meaningful data are essential.<sup>277</sup> Without reliable and sufficient information, it is impossible to make a statistical analysis for future projections regarding how to use PMCs more effectively in contingency operations. Furthermore, incomplete and inaccurate data on PMCs supporting stabilization and reconstruction campaigns may hamper planning and increase costs and risks. First, without accurate data, agencies cannot be sure how extensively they rely on contractors in carrying out their missions.<sup>278</sup> Second, without incorporating required data into planning efforts, agencies take unnecessary risks associated with their

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<sup>273</sup> Schwartz, "Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis," 20

<sup>274</sup> Ibid.

<sup>275</sup> Ibid.

<sup>276</sup> Ibid.

<sup>277</sup> Government Accountability Office, "Contingency Contracting: Further Improvements Needed in Agency Tracking of Contracting Personnel and Contracts in Iraq and Afghanistan," *GAO-10-187*, November 2, 2009, 1.

<sup>278</sup> Ibid.

missions.<sup>279</sup> Third, insufficient or wrong financial information on contracts can inhibit the creation of realistic budgets.<sup>280</sup> Finally, lack of insight may increase the likelihood of paying for duplicative services.<sup>281</sup>

In order to eliminate the negatives that stem from inaccurate and insufficient information about contractors, the Secretary of Defense, the Secretary of State, and the USAID signed a memorandum of understanding (MOU) about procedures for contracting in Iraq and Afghanistan as stated in Section 861 of the National Defense Authorization Act (NDAA) for FY2008. They created a system of record with regard to contract and contractor personnel information called the Synchronized Predeployment and Operational Tracker (SPOT).

The NDAA for FY2008 required the databases to track at a minimum:

- for each contract,
  - a brief description of the contract,
  - its total value, and
  - whether it was awarded competitively, and
- for contractor personnel working under contracts in Iraq or Afghanistan,
  - total number employed,
  - total number performing security functions, and
  - total number who have been killed or wounded.<sup>282</sup>

In this context, contracts with at least 14 days of duration in Iraq or Afghanistan, or valued more than \$100,000, would be entered into the SPOT, along with their personnel data. Elements, such as value and extent of competition, would be taken from the federal government's system of record on contracting, the Federal Procurement Data System – Next Generation (FPDS-NG), and added to the SPOT.

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<sup>279</sup> Government Accountability Office, "Contingency Contracting: Further Improvements Needed in Agency Tracking of Contracting Personnel and Contracts in Iraq and Afghanistan," *GAO-10-187*, November 2, 2009, 1.

<sup>280</sup> *Ibid.*, 1.

<sup>281</sup> *Ibid.*

<sup>282</sup> *Ibid.*, 2.

Previously, accessing required contracts and contractor personnel data was impeded due to some physical and methodological reasons. Particularly, data on contracts and contractor personnel in Iraq and Afghanistan was kept with the contractors, hoarded in multifarious data systems, or existed as hard copies in separate geographical regions. According to DoD, State and USAID officials, the use of SPOT has the potential to accumulate this scattered information to better regulate and supervise contractors.

The primary factor for deciding to enter contractor personnel into SPOT was whether a contractor needed a SPOT-generated letter of authorization (LOA). An LOA is an official document issued by a contracting officer to allow contractors to travel to, from, and within a designated area. It also identifies the privileges that the contractor has under the contract. Contractors need LOAs “to enter Iraq, receive military identification cards, travel on U.S. military aircraft, or, for security contractors, receive approval to carry weapons.”<sup>283</sup> However, local nationals in Iraq do not need LOAs and so they are not entered into SPOT. Moreover, the number of local nationals is inclined to fluctuate since most of them work on a daily basis, so are not always recorded by their contractors. Therefore, SPOT does not reflect the true number of local contractor personnel working in Iraq. In this respect, the SPOT system should be improved in a way that reveals more accurate data. The United States governmental agencies should address and coordinate issues regarding the entering local nationals and subcontractors into the SPOT because credible and meaningful data is essential for effective oversight and management.

### **3. Creating an Open, Transparent and Competitive Market**

There remain concerns about openness, transparency, and competency of the market in which PMCs operate. Although federal regulations on contracting promote neutral, competitive, open and transparent procedures, data indicates the opposite. For example, the testimony of David M. Walker points out that only 41 percent of DoD contracts in FY2005 were awarded through full competition.<sup>284</sup> Corruption is the natural

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<sup>283</sup> Government Accountability Office, “Contingency Contracting: Further Improvements Needed in Agency Tracking of Contracting Personnel and Contracts in Iraq and Afghanistan,” 6.

<sup>284</sup> David M. Walker, “DoD Acquisitions: Contracting for Better Outcomes,” *GAO Report GAO-06-800T*, September 7, 2006, 19.

consequence of any contract awarded without competition. Waste and fraud usually happen where institutional weaknesses are evident. In this regard, institutions play a key role in creating a competitive market that favors the principal.

From the principal's perspective, competition is required to minimize the costs, to prevent financial waste, to improve quality, and to encourage innovation. From the agent's perspective, competition is necessary to increase productivity and efficiency in the sector. However, PMCs often have incentives to eradicate competitiveness in order to gain a comparative advantage over their principals. Monopolization of certain services by several PMCs poses a serious jeopardy to competitiveness. As Martha Minow states, "When the government is the sole purchaser, a handful of contractors dominating the field often enjoys the power that undermines market efficiency and contractual accountability."<sup>285</sup> Enjoying the advantages that the monopoly provided, PMCs can use their bargaining power to exploit the government by simply determining the range of prices, the terms of contracts, and the way of conduct. For instance, the Halliburton Company was awarded the two largest contracts during OIF without competitive bidding, because there was simply no other option capable of providing the same services in the same scope and of the same quality.<sup>286</sup> Unless a competitive market discipline is established together with effective government oversight, PMCs can evade accountability without facing any difficulty.

Due largely to security considerations, Department of Defense contracts are mostly awarded to United States-based PMCs. The logic here is that awarding contracts to United States-based PMCs with great experience and successful past performance would not only strengthen the control arm of the state, but also economically benefit the internal private security market, making it stronger and more competitive than other markets. This implication may protect vital interests of the United States both at home and abroad, but it also puts some limitations on outsourcing, negatively affecting the competitiveness of the market. In some situations, such restrictions on conditions of

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<sup>285</sup> Minow, "Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy," 118.

<sup>286</sup> *Ibid.*, 115.

outsourcing may leave governmental agencies with unqualified or insufficient numbers of agents. Governmental agencies may come up against a contracting procedure in which the winner is predetermined. This is generally the case with PMCs that have strong ties with the United States government. Blackwater, Halliburton, KBR, MPRI, and Dyncorp, which have become highly specialized on certain goods and services over time, have dominated the market in the United States and become an oligopoly. Considering the extent of U.S. strategic objectives and that the requirements and restrictions on outsourcing benefit large United States-based corporations with strong ties, other PMCs in the market are placed in a disadvantageous position. Although some of these small PMCs are awarded subcontracts in Iraq and Afghanistan by bigger PMCs that constitute the oligopoly in the market, most of them have typically been awarded relatively small contracts at home, which provide comparatively lower profit margins. Therefore, the current system of contracting in the United States rewards big local corporations, while punishing small local corporations and PMCs based outside the United States. As Singer states, “such arrangements forget that the efficiency of privatization comes from greater competition, rather than simply that it is private.”<sup>287</sup>

Contrary to the common assumption that the private military industry is a very lucrative business, some scholars claim that it is not. For instance, Dew and Hudgens’ analysis shows that the private military industry is not as remunerative as expected.<sup>288</sup> They note that competition for contracts is so high that sometimes contracts leave no margin for profit.<sup>289</sup> They claim that much of the revenue is allocated to inside stakeholders (employees) who have a strong bargaining power in the competitive sector, leaving small margins of profit for the outside stakeholders and suppliers, who rely largely on the human capital of their employees.<sup>290</sup> Their findings make sense for markets where institutions are powerful to ensure competitiveness. However, their

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<sup>287</sup> Singer, *Corporate Warriors: the Rise of Privatized Military Industry*, 152.

<sup>288</sup> Dew and Hudgens, “Evolving Private Military Sector: A Survey,” 39.

<sup>289</sup> *Ibid.*, 40.

<sup>290</sup> *Ibid.*, 39–41.

findings are apparently not valid for markets that are dominated by institutional weaknesses and corruption. This is particularly the case in failed states, which host contingency operations within their territories.

If there are institutional mechanisms that are capable of guaranteeing a competitive market, principals enjoy such benefits as cost efficiency and greater control. On the other hand, the contracts awarded without competition always run the risk of overcharge and fraud. Predictably, markets in the United States would produce better outcomes for the public, whereas markets in Iraq and Afghanistan would generate relatively poorer outcomes. This is largely because the market in the United States is better regulated than both that of Iraq and that of Afghanistan. In this sense, contingencies are risky and uncertain environments that negatively affect the competitiveness of the market. When there are only a couple of PMCs qualified to provide a particular service under highly unpredictable and complex circumstances, contracts usually leave these PMCs huge margins of profit.

As discussed in the previous chapter, markets create their own dynamics. All participants continuously shape the market, affecting the way it works. Governmental agencies, which are the clients of the market, and PMCs, which are the sellers of various goods and services to their clients, have a direct impact on the way the market works. Governmental agencies put restrictions on the conduct, and determine the time, quantity, and quality of the delivery. On the other hand, in order to win the contract, PMCs, compete with each other to provide the goods or services that the client demands at minimum cost. Besides the effects on competitiveness, and the effectiveness and efficiency of firms, markets also influence the way firms operate, affecting the behavior of PMCs. If structural mechanisms promote successful PMCs with a clean past and high performance, other PMCs would begin to adopt similar principles and norms. If reputation becomes an important consideration, PMCs begin to follow more transparent methods. In this sense, markets, if open, transparent and competitive, begin to regulate PMCs, pushing them to follow more humanitarian techniques and tactics.

#### **4. Strengthening Interagency Coordination Mechanisms**

The presence of an interagency coordination mechanism in a contingency operation that is authorized monitor and report the activities of the government's de facto agents would likely to increase control over PMCs. Moreover, such mechanisms would not only deter PMCs from shirking and breaching laws and norms, but also increase effectiveness and efficiencies of governmental agencies. Thus far, the Department of Defense created Contractor Operations Cells in Iraq and Afghanistan to coordinate the activities of PMCs.<sup>291</sup> Furthermore; the DoD established the Army Contractor Oversight Directorate and charged it with the task of the investigation of the use of force by PMCs and the development of policies in this regard.<sup>292</sup> A report issued by SIGIR in July 2009, states that recent institutional and procedural adjustments such as the memorandum of agreement (MOA) between Department of Defense and Department of State and the creation of ACOD, have improved the control and coordination of PMCs' activities in Iraq.<sup>293</sup> However, governmental agencies have less control over PMCs in Afghanistan, since ACOD in Afghanistan is relatively a new organization, which is currently trying to evolve into a more mature institution. Furthermore, unlike ACOD in Iraq, whose personnel are mostly the government officials; most of the staff of ACOD in Afghanistan is comprised of contractors, rather than government officials. These shortcomings lead to inefficiencies on the part of governmental agencies that hire PMCs. These weaknesses should be eliminated, and interagency coordination mechanisms should be strengthened. In this regard, first and foremost, the current problems within SPOT should be solved. Control over PMCs in a contingency operation is only as good as the information upon which interagency coordination mechanisms rely. Second, the function of coordination of PMCs should not be outsourced to PMCs. Hiring a PMC for supervision of other PMCs would not only provide this company with unfair competition leverage, but would also

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<sup>291</sup> Schwartz, "Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis," 15.

<sup>292</sup> Commission on Wartime Contracting in Iraq and Afghanistan, "At what Cost? Contingency Contracting in Iraq and Afghanistan," 73.

<sup>293</sup> Office of the Special Inspector General For Iraq Reconstruction, "Field Commanders See Improvements in Controlling and Coordinating Private Security Contractor Missions in Iraq," *SIGIR Report 09-22*, July 28, 2009, 5.

undermine the government's direct control over activities of PMCs in contingency operations. Last, interagency coordination mechanisms should cooperate with the local government to increase the quality of regulation.

## **5. Increasing the Quality and Quantity of Contracting Professionals**

The report of Commission on Wartime Contracting in Iraq and Afghanistan states that the level of need for CORs changes in line with the complexity of the contract: while expensive service contracts with a broad scope that requires a considerable technical and scientific proficiency may necessitate full-time CORs, single-service contracts with a short period and a low dollar-value may obligate no COR monitoring.<sup>294</sup> Keeping these different needs in mind, the United States should estimate the actual required capacity to better monitor contracts with PMCs in contingency operations. Presumably, greater number of CORs and COs would lead to better contract management and less financial and conduct related abuses, but only if they are properly trained to monitor and manage PMCs during contingencies. The United States should also provide their contracting personnel with adequate pre-deployment training and ongoing contingency contracting training. These measures would bring about greater control, less fraud and more efficiency on the part of governmental agencies, while preventing and deterring PMCs from shirking.

Officials state that the Department of Defense already began to improve the workforce acquisition numbers in Iraq and Afghanistan.<sup>295</sup> In May 2009, the Secretary of Defense issued a plan that will gradually increase the size of the acquisition workforce.<sup>296</sup> In accordance with this plan, Department of Defense officials expect the acquisition workforce to gain 20,000 contracting professionals by 2015.<sup>297</sup> If this plan

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<sup>294</sup> Commission on Wartime Contracting in Iraq and Afghanistan, "At what Cost? Contingency Contracting in Iraq and Afghanistan," 9.

<sup>295</sup> Ibid.

<sup>296</sup> Ibid.

<sup>297</sup> Ibid.



materializes, the oversight arm of the Department of Defense may gain strength and existing monitoring problems with respect to insufficiency of contracting professionals may be largely resolved.

## **6. Training Commanders and Clarifying Authorities**

Military officers on the ground often do not know whether and how they can control PMCs. Furthermore; commanders are confused about where their authority over private military personnel begins and ends. By and large, this confusion stems from an incompatible blend of authorities and responsibilities that manage PMCs in contingency operations. Private military personnel mainly operate under two different authorities in contingencies: the authority of their civilian supervisors, and the authority of the commander whom they support. On the one hand, the incorporation of private military personnel into the military structure requires private military personnel to follow the orders of the military commanders. On the other hand, private military personnel are hired and fired by their civilian superiors. This tension creates vague lines of authority with respect to who really have the right to manage them. Moreover, PMCs are generally expected to conform to the same general rules and procedures as militaries, but there are times they do not. Although contractors are subject to the same laws as military personnel, conventional wisdom says that in comparison to military personnel, private military personnel is more likely to be exempt from prosecution. As Minow states, “Even if the lines of authority clearly locate the civilian contractor employees under military command, these civilians do not face the same rewards and sanctions as do the members of the military, including military culture and command structure.”<sup>298</sup> In 2007, the U.S. Congress extended the Uniform Code of Military Justice (UCMJ) to encompass the employees of PMCs that accompany the U.S. military in contingency operations. According to Senator Lindsey Graham, this modification of the UCMJ would be helpful in terms of facilitating commanding contractors by providing commanders on the ground

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<sup>298</sup> Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” 121.

with “a more fair and efficient means of discipline” during contingency operations.<sup>299</sup> However, expansion of the UCMJ has raised many issues; the most critical of which is whether it is appropriate to expose civilian contractors to the military justice system. Another issue that scholars often raise is whether the U.S. Congress has the authority to order the prosecution of civilians under military discipline. If we consider the answers to the previous issues as positive, who would be responsible to prosecute them? What will happen if the principal deliberately overlooks contractors’ breaching of law? Finally, would civilian contractors also be subject to the articles in regard to command structure and military honor? Thus, confusion remains.

A Congressional Research Service Report published in July 2010, states that in response to findings of the Gansler Report, the Department of Defense has taken many steps to improve the training level of uniformed personnel that are assigned to supervise PMCs in contingency operations.<sup>300</sup> The report notes that the Department of Defense is already working on an online course that provides military personnel with pre-deployment training with respect to the management of contractors during military operations.<sup>301</sup> Furthermore, it reports that the Department of Defense intends to incorporate courses regarding contract support into the training process of non-acquisition personnel, and the United States Army continues to develop instructive handbooks in order to assist military personnel in learning how to better coordinate and work with PMCs in contingencies.<sup>302</sup> Even though DoD has taken some steps to improve the level of training of its military personnel, additional actions are needed to address remaining concerns.<sup>303</sup>

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<sup>299</sup> William Matthews, “Contractor Crackdown,” *Armed Forces Journal*, February 2007, at: <http://www.afji.com/2007/02/2471808/> (accessed August 11, 2010).

<sup>300</sup> Schwartz, “Department of Defense Contractors in Iraq and Afghanistan: Background and Analysis,” 14.

<sup>301</sup> Ibid.

<sup>302</sup> Ibid.

<sup>303</sup> U.S. Government Accountability Office, “DoD Needs to Reexamine Its Extensive Reliance on Contractors and Continue to Improve Management and Oversight,” *GAO-08-572-T*, March 11, 2008, Highlights Page.

In order to better supervise PMCs, in addition to exposing military personnel to proper and adequate training prior to deployment, ongoing training that follows predeployment training is essential to keep military personnel updated. This training should be repeated on a regular basis during the deployment period. Importantly, they should be given clear instructions on how to manage private military personnel on the ground. Governmental agencies should obligate PMCs that work for the United States government in contingency operations, to train their personnel on these issues as well. Private military personnel should also be given clear instructions as to who has the authority to manage them during their missions. They should be warned about possible consequences of their misconduct or disobedience. The United States should punish perpetrators as necessary to signal that breaches by private military personnel will not be tolerated.

## **7. Continuing to Use the Licensing System**

In order to protect its national interests in contingency operations, the U.S. has been using a licensing system to regulate PMCs in Iraq and Afghanistan under the U.S. Arms Export Control Act, which “provides the authority to control the export of defense articles and services.”<sup>304</sup> PMCs, which are located in the United States but offer military advice to foreign nationals in contingency operations, are obliged to register with, and get a license from, the Department of State “under the International Transfer of Arms Regulations (ITAR), which implement the Arms Export Control Act.”<sup>305</sup> The licensing system is an effective tool to push PMCs to embrace similar international norms and standards. In this regard, while directly managing PMCs with contracts, the United States should also increase the standards required to obtain a license. Furthermore, the United States should monitor PMCs that are registered in the United States but operate in Iraq and Afghanistan, even if they work independently from the United States government, and cancel the licenses of PMCs whose misconduct is proven.

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<sup>304</sup> See Arms Export Control Act, at: [http://www.pmddtc.state.gov/regulations\\_laws/aeca.html](http://www.pmddtc.state.gov/regulations_laws/aeca.html) (accessed August 9, 2010).

<sup>305</sup> Fred Schreier and Marina Caparini, “Privatizing Security: Law, Practice and Governance of Private Military and Security Companies,” *paper (Occasional Paper No: 6) presented as part of the policy dialogue on issues pertaining to the core mission of Geneva Centre for the Democratic Control of Armed Forces (DCAF) in Geneva*, March 2005, 105.

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## **IV. REGULATING PRIVATE MILITARY COMPANIES**

### **A. BACKGROUND**

In this chapter, some underlying problems regarding regulating PMCs in contingency operations will be examined to better understand how the current regulatory framework exempts private military personnel from prosecution in some cases. It will be discussed how PMCs may undermine stabilization and reconstruction efforts when they are not regulated properly.

Today, some scholars see PMCs as a crucial part of the U.S. strategy in Iraq and Afghanistan; however, others worry about their possible negative influences on the United States' stabilization and reconstruction efforts.<sup>306</sup> Jennifer K. Elsea articulates these concerns as follows, "Due to a spate of high-profile incidents involving contractors allegedly shooting civilians, using excessive force, committing other crimes, or otherwise behaving in a manner that may be offensive to the local population, there is concern that the reliance on contractors may be undermining U.S. counterinsurgency efforts in Iraq and Afghanistan."<sup>307</sup> In the last decade, transparency and accountability of PMCs, and the problematic legal framework in which they operate, have been debated at length in various reports published by the CBO, GAO, and CRS, as well as in books, articles and

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<sup>306</sup> Elsea, "Private Security Contractors in Iraq and Afghanistan," Summary.

<sup>307</sup> *Ibid.*, 1.

journals written by different scholars, analysts, and contract law specialists.<sup>308</sup> Some scholars, such as Jennifer K. Elsea, Michael John Garcia, R. Chuck Mason, Jackson Nyamuya Maogoto, Benedict Sheehy, Doug Brooks, Marina Caparini, Mosche Schwartz, Marc Lindemann, and Kennon H. Nakamura, examined which laws regulate PMCs in armed conflicts, as utilization of PMCs by states, and international and regional organizations has increased dramatically.

Though their opinions about which functions should be carried out by PMCs or how PMCs should be monitored and managed differs more or less, scholars generally agree that the problematic legal framework in which PMCs operate poses many challenges in terms of their use in contingency operations, since the current regulatory framework exempts private military personnel from prosecution in particular cases. On the one hand, there are international laws that establish a vague framework but are not useful for defining the current activities and roles of PMCs in contingency operations. On the other hand, there are national laws, which are unable to regulate PMCs effectively, either because of insufficient capacity or political unwillingness. In this sense, the enforcement problem of international law, insufficient capacities of Iraq and Afghanistan, and political unwillingness of the United States, coupled with the highly changing characteristic of contingency environments, provide PMCs with considerable flexibility in terms of their legal obligations and practices.

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<sup>308</sup> Elsea, "Private Security Contractors in Iraq and Afghanistan," Summary, 1–29, Isenberg, *Shadow Force: Private Security Contractors in Iraq*, 105–157, Isenberg, "Private Military Contractors and U.S. Grand Strategy," 9–41, Avant, *The Market Force: the Consequences of Privatizing Security*, 3–265, Elsea et.al., "Private Security Contractors in Iraq: Background, Legal Status and Other Issues," 14–50, Marc Lindemann, "Civilian Contractors under Military Law," *Parameters*, Autumn 2007, 83–93, Bruneau, n.d. *For Patriotism or Profit: Soldiers, Contractors and the U.S. Civil Military Relations* 231–264, Department of Defense, "Investigation of Intelligence Activities At Abu Ghraib," 52, Brayton, "Outsourcing War: Mercenaries and the Privatization of Peacekeeping," 322, Cleaver, *Subcontracting military power: The privatization of security in contemporary Sub-Saharan Africa* 141, Dumlupinar, "Regulation of Private Military Companies in Iraq," 31–93, John R. Luckey et al., "Inherently Governmental Functions and Department of Defense Operations: Background, Issues, and Options for Congress," 1–58, Singer, *Corporate Warriors: The Rise of the Privatized Military Industry*, 151–245, Carafano, *Private Sector, Public Wars: Contractors in Combat, Afghanistan, Iraq and Future conflicts*, 47–105, Schreier and Caparini, "Privatizing Security: Law, Practice and Governance of Private Military and Security Companies" 150, Marina Caparini, "Regulating Private Military and Security Companies: The US Approach," an article from the book *Private Military and Security Companies: Ethics, Policies and Civil-Military Relations*, (New York: Routledge, 2008), 171–184, Doug Brooks and Matan Chorem, "Ruthless Humanitarianism: Why marginalizing private peacekeeping kills people," in Andrew Alexandra, Deana-Peter Baker and Marina Caparini eds., *Private Military and Security Companies* (New York: Routledge, 2008), 116–128.

Some scholars claim that PMCs generally carry out tasks defensive in nature, so there should be no concern that they may damage stabilization and reconstruction efforts in contingency operations. International humanitarian law, however, does not distinguish between offensive and defensive operations.<sup>309</sup> What is important, as a matter of international law, is whether or not there is direct participation in hostilities. From this perspective, it is obvious that PMCs may face situations in which they have to use force, even if they are hired to perform static security tasks such as base security or building security.<sup>310</sup> Defensive operations do not necessarily mean that PMCs will never participate in direct hostilities. Furthermore, since they frequently work in close proximity to military personnel, they may be the victims of collateral damage, even if they do not carry weapons or use force.<sup>311</sup> It is even more difficult to determine which functions are defensive and which are offensive in contingency operations where the line between service missions and combat missions often blurs. In both Iraq and Afghanistan, private military personnel, who mostly execute service missions, have become as vulnerable as military personnel who perform combat operations. Moreover, some PMCs have performed missions that were previously executed only by lawful combatants.<sup>312</sup> While executing these tasks, many PMC personnel have faced situations that compelled them to use force in Iraq and Afghanistan. Today, it is difficult to consider any military or private military missions independent of each other because the complexity of the operational environment has led private military missions to overlap with military missions.

Many of the complications regarding prosecution of private military personnel stem from their murky legal status under international humanitarian law. International humanitarian law does not provide PMCs themselves with a status, but it does so for their

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<sup>309</sup> Emanuela-Chiara Gillard, "Private Military/Security Companies: the Status of Their Staff and Their Obligations under International Humanitarian Law and The Responsibilities of States in Relation to Their Operations," in *Private Military and Security Companies: Ethics, Policies and Civil-Military Relations*, Andrew Alexandra, Deana-Peter Baker and Marina Caparini eds., (New York: Routledge, 2008), 165.

<sup>310</sup> Ibid.

<sup>311</sup> Ibid.

<sup>312</sup> Lindemann, "Civilian Contractors under Military Law," 84.

staff.<sup>313</sup> However, even though personnel of PMCs have a status under international humanitarian law, their status may change depending on the nature of their contract and of the functions they carry out.<sup>314</sup> This complication requires that their status be determined on a case-by-case basis.<sup>315</sup> For example, according to the Fourth Geneva Convention, Blackwater employees, who were killed and hanged on a bridge in Fallujah in 2004, were not non-combatants, since they were carrying weapons.<sup>316</sup> On the other hand, they were not lawful combatants under the Third Geneva Convention, as they were not wearing uniforms and did not have an organic tie to the command structure of the military.<sup>317</sup> According to international law, they were not mercenaries either, because mercenaries are defined as combatants whose country is not a party to the conflict and who fight for a foreign government.<sup>318</sup> Similarly, in 2003, guerillas kidnapped three contractor personnel working for California Microwave Systems after their airplane crashed in Colombia. Although hired by the United States Navy, they were not treated as prisoners-of-war because the Geneva Conventions exempted them from the rights of lawful combatants.<sup>319</sup>

The International Community of the Red Cross (ICRC) embarked on a new initiative to remind states and PMCs of their existing legal responsibilities. Thanks to constructive efforts of Switzerland's government and the ICRC, the Montreux Document was signed in October 2009 by seventeen countries that widely deal with PMCs as either contracting states, territorial states or home states, to develop "best practices" with regard to the proper use of PMCs. For now, the Montreux Document appears to be the only

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<sup>313</sup> Gillard, "Private Military/Security Companies: the Status of Their Staff and Their Obligations under International Humanitarian Law and the Responsibilities of States in Relation to Their Operations," 160.

<sup>314</sup> Ibid.

<sup>315</sup> Lindsey Cameron, "Private military companies: Their status under international humanitarian law and its impact on their regulation," *International Review of the Red Cross*, Vol.88, No. 863, September 2006, 578, available at: [http://www.icrc.org/Web/eng/siteeng0.nsf/htmlall/review-863-p573/\\$File/irrc\\_863\\_Cameron.pdf](http://www.icrc.org/Web/eng/siteeng0.nsf/htmlall/review-863-p573/$File/irrc_863_Cameron.pdf) (accessed on August 10, 2010).

<sup>316</sup> Stanger, *One Nation Under Contract*, 106.

<sup>317</sup> Ibid.

<sup>318</sup> Ibid.

<sup>319</sup> Ibid., 92.



international document that covers PMCs.<sup>320</sup> It is the most comprehensive and promising attempt to regulate PMCs at the international level so far; however, it is not a binding, but a recommendatory document. As a result, enforcement is still a considerable challenge in terms of international law, since there is no overarching authority in the international system; therefore, we have nothing to rely on but national laws to regulate PMCs.

The United States' past experiences with PMCs in Iraq and Afghanistan point out the various challenges and complexities of prosecuting PMC personnel in certain situations. Currently, private military personnel, who accompany United States military overseas, are subject to either the Military Extraterritorial Jurisdiction Act (MEJA) or the Uniform Code of Military Justice (UCMJ), depending on the nature of their crime or violation.<sup>321</sup> Since PMCs perform a wide variety of functions under different conditions and circumstances, it is unclear in which category private military personnel should be assessed. Scholars and law specialists suggest that rather than applying a static and general regulatory framework to cover all PMC personnel regardless of their nature of contracts, incidents in which private military personnel participated should be taken into consideration on a case-by-case basis to determine which law applies. Although an extension of the UCMJ in 2007 to cover contractors accompanying the United States military in contingency operations has facilitated the prosecution of private military personnel for certain crimes, application of the UCMJ still looks problematic.

This chapter will examine major international conventions and documents, and domestic laws in the United States, Iraq and Afghanistan that regulate PMCs in contingency operations to better understand the challenges of keeping PMCs accountable. It will be discussed that states still have non-transferable obligations, even if they delegate their authority by contracting with a PMC, and states may lose control over PMCs if they do not use effective punishment mechanisms.

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<sup>320</sup> Elsea, "Private Security Contractors in Iraq and Afghanistan: Legal Issues," 9.

<sup>321</sup> *Ibid.*, 18.

## B. LEGAL FRAMEWORK

According to a 2009 CRS report, United States contractors in Iraq and Afghanistan operate under three levels of regulation: international laws, the United States law, and the domestic laws of host countries.<sup>322</sup>

### 1. International Law

#### a. *Geneva Conventions*

The question of whether staffs of PMCs are civilians or combatants is central to the regulation of PMCs, since international humanitarian law applies to each status differently. If they have a combatant status, they may be targeted in an armed conflict and thus are entitled to the rights of lawful combatant status.<sup>323</sup> On the other hand, if they have a civilian status, then other parties cannot attack them. If they directly participate in hostilities despite their civilian status, they lose their immunity from being targeted, and if they are captured, they are not entitled to prisoner-of-war status.<sup>324</sup>

The Geneva Conventions, which are the only globally accepted laws regarding mercenaries, defines private military personnel as “noncombatant personnel who accompany combatant forces.”<sup>325</sup> The Third Geneva Convention provides civilian personnel accompanying the armed forces with a prisoner-of-war status. According to Article 4 of the Third Geneva Convention:

Persons who accompany the armed forces without actually being members thereof, such as civilian members of military aircraft crews, war correspondents, supply contractors, members of labour units or of services responsible for the welfare of the armed forces, provided that they have received authorization from the armed forces which they accompany, who shall provide them for that purpose with an identity card similar to the annexed model.<sup>326</sup>

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<sup>322</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: Legal Issues,” 2.

<sup>323</sup> Gillard, “Private Military/Security Companies: the Status of Their Staff and Their Obligations under International Humanitarian Law and the Responsibilities of States in Relation to Their Operations,” 162.

<sup>324</sup> Ibid.

<sup>325</sup> See Third Geneva Convention, Article 4 (4), at: <http://www.icrc.org/ihl.nsf/FULL/375?OpenDocument> (accessed on August 7, 2010)

<sup>326</sup> Ibid.

The abovementioned personnel are not combatants but will be treated as prisoners of war upon capture. Unquestionably, the staffs of PMCs that accompany the United States military in Iraq and Afghanistan to carry out support functions fall within this category.<sup>327</sup> Nevertheless, it appears that personnel of PMCs that are working for the United States military in these countries to execute combat related tasks, for which they have to carry weapons and are likely to use force, do not fall within this category.<sup>328</sup>

Another important question that must be addressed to better comprehend the position of PMCs in terms of international law is whether the staffs of PMCs are mercenaries or lawful combatants. This question is significant, since international law provides mercenaries and lawful combatants with different statuses, different obligations, and different rights. While international law give the members of armed forces of states the right of taking part in hostilities in an armed conflict and the right to be treated as prisoners-of-war, it does not allow mercenaries to participate in hostilities directly, and deprives mercenaries of the benefits of being treated as prisoners-of-war.<sup>329</sup> However, this does not mean that international law does not protect mercenaries.<sup>330</sup> The Fourth Geneva Convention protects mercenaries, like all other civilians in an armed conflict, obligating all parties to the conflict to treat mercenaries humanely, and requiring the protection of minimum humanitarian and judicial rights once they are captured.<sup>331</sup>

At that point, how mercenaries are conceptualized by international law is essential to drawing the distinction between different statuses of mercenaries and lawful combatants. Article 47 of Additional Protocol to Geneva Conventions presents the following definition of mercenaries:

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<sup>327</sup> Gillard, "Private Military/Security Companies: the Status of Their Staff and Their Obligations under International Humanitarian Law and the Responsibilities of States in Relation to Their Operations," 163.

<sup>328</sup> Ibid., 164.

<sup>329</sup> Ibid., 161.

<sup>330</sup> Ibid.

<sup>331</sup> See The Fourth Geneva Convention at: <http://www.icrc.org/ihl.nsf/full/380?opendocument> (accessed on August 7, 2010).

1. A mercenary shall not have the right to be a combatant or a prisoner of war.
2. A mercenary is any person who:
  - (a) Is specially recruited locally or abroad in order to fight in an armed conflict;
  - (b) Does, in fact, take a direct part in the hostilities;
  - (c) Is motivated to take part in the hostilities essentially by the desire for private gain and, in fact, is promised, by or on behalf of a Party to the conflict, material compensation substantially in excess of that promised or paid to combatants of similar ranks and functions in the armed forces of that Party;
  - (d) Is neither a national of a Party to the conflict nor a resident of territory controlled by a Party to the conflict;
  - (e) Is not a member of the armed forces of a Party to the conflict; and
  - (f) Has not been sent by a State which is not a Party to the conflict on official duty as a member of its armed forces.<sup>332</sup>

The abovementioned definition of mercenaries establishes six clear criteria for determining whether or not a particular person is a mercenary. Now, let us turn to our primary question: Are the staffs of PMCs mercenaries or are they lawful combatants? The answer to this question is not an easy one, since personnel of PMCs perform different tasks under different mandates in contingency operations. While some of them work directly for governmental agencies, others are doing their business independent of contracting or territorial states. Some personnel are directly contracted by states, whereas others are subcontractors of another PMC, which directly works for a contracting state, territorial state, or a home state. There are also third party countries, international and regional organizations, NGOs, and private corporations that hire PMCs to carry out certain tasks. Some carry weapons and wear distinctive uniforms, while others simply look like civilian personnel. Therefore, given the six aforementioned criteria, it is quite difficult to decide whether or not PMCs are mercenaries because not all private military personnel fall specifically into the area that is described by Protocol I to the Geneva Conventions. There are chiefly three reasons. First, locals, who make up a significant

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<sup>332</sup> Protocol Additional to the Geneva Conventions of 12 August 1949 and relating to the Protection of Victims of International Armed Conflicts (Protocol I), Part 3, Article 47.

portion of the total workforce of PMC, constitute a party to the conflict.<sup>333</sup> For example, as of September 2009, local nationals comprised about 90 percent of the total armed security contractors in Afghanistan.<sup>334</sup> Second, most of them do not directly take part in hostilities.<sup>335</sup> According to a CRS report, as of September 2009, while armed private security contractors in Iraq and Afghanistan constituted 10 percent of all contractors, they comprised only 5 percent of the Department of Defense's workforce.<sup>336</sup> The rest were basically not carrying weapons while performing their missions and mostly employed to execute logistical tasks, life support functions, or basic reconstruction works. Finally, since all the criteria must be satisfied in order to name an entity as a mercenary, it is quite problematic to decide whether or not a particular contractor is a mercenary under the Article 47 of the Geneva Conventions.

Mercenarism is defined and prohibited by two primary laws: The Convention for Elimination of Mercenarism in Africa, and The U.N. International Convention Against the Recruitment, Use, Financing, and Training of Mercenaries. The former is a regional attempt to prevent mercenary activity, while the latter is an international attempt. According to Article 1 of The Convention for Elimination of Mercenarism in Africa:

1. The crime of mercenarism is committed by the individual, group, or association, representatives of a State and the State itself with the aim of opposing by armed violence a process of self-determination or the territorial integrity of another State that practices any of the following acts:

- a) Shelters, organizes, finances, assists, equips, trains, promotes supports or in any manner employs armed forces partially or wholly consisting of persons who are not nationals of the country where they are going to act, for personal gain, material or otherwise;
- b) Enlists, enrolls or tries to enroll in the said forces;

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<sup>333</sup> Isenberg, "Private Military Contractors, and U.S. Grand Strategy," 10.

<sup>334</sup> Schwartz, "The Department of Defense's Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress," 8.

<sup>335</sup> Isenberg, "Private Military Contractors, and U.S. Grand Strategy," 10.

<sup>336</sup> Schwartz, "The Department of Defense's Use of Private Security Contractors in Iraq and Afghanistan: Background, Analysis, and Options for Congress," 7.

c) Allows the activities mentioned in paragraph (a) to be carried out in any territory under its jurisdiction, or in any place under its control, or affords facilities for transit, transport, or other operations of the abovementioned forces.

2. Any person, natural or juridical who commits the crime of mercenarism as defined in paragraph 1 of this Article commits an offence considered as a crime against peace and security in Africa and shall be punished as such.<sup>337</sup>

The mercenary definition of the Convention for Elimination of Mercenarism in Africa is similar to that of Article 47 of Additional Protocol of Geneva Conventions. The convention prohibits its nationals from mercenary activity; however, the enforcement mechanism of the convention does not work properly and is incapable of punishing mercenaries particularly operating abroad.

Article 1 of The U.N. International Convention Against the Recruitment, Use, Financing, and Training of Mercenaries defines mercenaries as follows:

1. A mercenary is any person who:
  - (a) Is specially recruited locally or abroad in order to fight in an armed conflict;
  - (b) Is motivated to take part in the hostilities essentially by the desire for private gain and, in fact, is promised, by or on behalf of a party to the conflict, material compensation substantially in excess of that promised or paid to combatants of similar rank and functions in the armed forces of that party;
  - (c) Is neither a national of a party to the conflict nor a resident of territory controlled by a party to the conflict;
  - (d) Is not a member of the armed forces of a party to the conflict; and
  - (e) Has not been sent by a State, which is not a party to the conflict on official duty as a member of its armed forces.
2. A mercenary is also any person who, in any other situation:
  - (a) Is specially recruited locally or abroad for the purpose of participating in a concerted act of violence aimed at:

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<sup>337</sup> See “The Convention of Organization of African Unity (OAU) for Elimination of Mercenarism in Africa,” [http://www.iss.co.za/uploads/CONVENTION\\_ON\\_MERCENARIES.PDF](http://www.iss.co.za/uploads/CONVENTION_ON_MERCENARIES.PDF), (accessed July 5, 2010).

(i) Overthrowing a Government or otherwise undermining the constitutional order of a State; or

(ii) Undermining the territorial integrity of a State;

(b) Is motivated to take part therein essentially by the desire for significant private gain and is prompted by the promise or payment of material compensation;

(c) Is neither a national nor a resident of the State against which such an act is directed;

(d) Has not been sent by a State on official duty; and

(e) Is not a member of the armed forces of the State on whose territory the act is undertaken.<sup>338</sup>

The mercenary definition of The U.N. International Convention Against the Recruitment, Use, Financing, and Training of Mercenaries is taken from the Geneva Conventions and expanded by adding a few sentences to restrict the utilization of PMCs in weak states for the purpose of overthrowing a government or weakening the unity of a State. According to Article 5 of the convention:

1. States Parties shall not recruit, use, finance or train mercenaries and shall prohibit such activities in accordance with the provisions of the present Convention.

2. States Parties shall not recruit, use, finance or train mercenaries for the purpose of opposing the legitimate exercise of the inalienable right of peoples to self-determination, as recognized by international law, and shall take, in conformity with international law, the appropriate measures to prevent the recruitment, use, financing or training of mercenaries for that purpose.<sup>339</sup>

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<sup>338</sup> See Article 1 of The U.N. International Convention Against the Recruitment, Use, Financing and Training of Mercenaries prohibits the Recruitment, Use, Financing and Training of Mercenaries, at: <http://www.un.org/documents/ga/res/44/a44r034.htm>, (accessed July 5, 2010).

<sup>339</sup> See The U.N. International Convention Against the Recruitment, Use, Financing, and Training of Mercenaries, Article 5, at: <http://www.un.org/documents/ga/res/44/a44r034.htm> (accessed August 24, 2010).

The U.N. International Convention Against the Recruitment, Use, Financing and Training of Mercenaries prohibits the recruitment, use, financing and training of mercenaries; however, there is also no monitoring or enforcement mechanism, so the application and implication rely on individual member states.<sup>340</sup>

***b. The Montreux Document***

The U.S. and sixteen other countries, including Iraq and Afghanistan, signed the Montreux Document on October 8, 2009 to develop “best practices” regarding the utilization of PMCs.<sup>341</sup> Even though the Montreux Document is not a legally binding instrument, it provides a rather comprehensive and useful framework for regulating PMCs in contingency operations. It not only “provides states with good practices,” but also promotes “compliance with international humanitarian law and human rights law during armed conflict.”<sup>342</sup> In short the document requires contracting states to be responsible under international law and not to contract out certain functions.<sup>343</sup> The document also lists responsibilities of territorial states, home states, and PMCs themselves, and recommends proper practices to them.

Part one of the document recalls pertinent international legal obligations and responsibilities of relevant states and PMCs themselves. It highlights that contracting states have non-transferable responsibilities; therefore, their obligations remain under international law, even if they hire PMCs to perform functions that belong to the state itself.<sup>344</sup> The document reminds States that international law prohibits contracting inherently governmental functions out, like “supervision of prisoner-of-war camps and

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<sup>340</sup> Schreier and Caparini, “Privatizing Security: Law, Practice and Governance of Private Military and Security Companies,” 150.

<sup>341</sup> UN Document A/63/467-S/2008/636 (October 8, 2009), at: [http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/\\$FILE/Montreux-Documents-eng.pdf](http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/$FILE/Montreux-Documents-eng.pdf). (accessed March 22, 2010).

<sup>342</sup> See the Montreux Document, preface, at: [http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/\\$FILE/ICRC\\_002\\_0996.pdf](http://www.icrc.org/web/eng/siteeng0.nsf/htmlall/montreux-document-170908/$FILE/ICRC_002_0996.pdf) (accessed July 19, 2010).

<sup>343</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan,” 9.

<sup>344</sup> See the Montreux Document, 32.



civilian places of internment.”<sup>345</sup> According to the document, states should decide which services are inherently governmental and which services are commercial, taking into consideration whether outsourcing a particular service would lead the PMC to take part directly in hostilities.<sup>346</sup> The Geneva Convention obligates states not only to abstain from committing human rights crimes and violations, but also to take all precautions in their power to prevent their de facto agents, like PMCs, to conduct such abuses.<sup>347</sup> Elsea summarizes the non-transferable responsibilities of states that are mentioned in the second part of the document as follows:

Further, contracting states are obligated to ensure that contractors are aware of their obligations and trained accordingly; to take appropriate measures to prevent any violations of international humanitarian law by private military and security company personnel; to adopt appropriate military regulations, administrative orders or other regulatory measures as well as administrative, disciplinary or judicial sanctions, as appropriate; to prevent, investigate and provide effective remedies for relevant misconduct of private military and security companies and their personnel; and to enact any legislation necessary to provide effective penal sanctions for grave breaches of the Geneva Conventions and other crimes in violation of international law, and to pursue prosecutions in case of such a breach or permit the host country or an international tribunal to do so.<sup>348</sup>

Part two of the document lists some good practices with respect to PMCs. The Montreux Document maintains that contracting states have the power to influence how PMCs perform their missions in the field.<sup>349</sup> In this respect, states should establish transparent and supervised contracting procedures;<sup>350</sup> adopt selection criteria that force PMCs and their subcontractors to obey international norms;<sup>351</sup> set prerequisites, such as possession of necessary authorizations, sufficient training regarding human rights law, legal and proper use of weapons and equipment, satisfactory internal policies, employee

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<sup>345</sup> See the Montreux Document, 32.

<sup>346</sup> Ibid., 33.

<sup>347</sup> Ibid.

<sup>348</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: Legal Issues,” 9–10.

<sup>349</sup> See the Montreux Document, 33.

<sup>350</sup> Ibid., 17.

<sup>351</sup> Ibid.

and property records, and clean history of past conduct to ensure that PMCs working for States meet basic requirements;<sup>352</sup> require PMC personnel to wear identifiable uniforms that are quite distinct from militaries when executing their missions;<sup>353</sup> monitor compliance of PMCs to contracts and maintain accountability of PMCs.<sup>354</sup>

The United States and other countries that widely use PMCs may use the Montreux Document as a guide to regulate PMCs. The document is also applicable to home states and territorial states such as Iraq and Afghanistan. These states may use the document as an instrument to establish effective control over PMCs. It also recalls that employees of PMCs are bound by international humanitarian law, human rights law, and other international documents; hence, they should adhere to international norms regardless of their status, particularly during armed conflicts.

After examining international documents and conventions, next we will turn to relevant national laws. According to Brooks and Chorev, “it is the ultimate responsibility of states to write laws, carry out criminal proceedings, make policies and draw the ethical boundary lines that need to be drawn.”<sup>355</sup> Keeping that in mind, the rest of the chapter will seek to find the weaknesses of existing national regulations and will try to answer the question of how contracting and territorial states can better regulate PMCs in contingency operations. For the purpose of this thesis, only three national regulations regarding PMCs will be discussed: United States laws, Iraqi Law, and Afghanistan Law.

## **2. National Laws**

In the United States, there are mainly two domestic laws that can be used to judge contractors: MEJA and UCMJ. In the current situation, in accordance with the Withdrawal Agreement between the United States and the Iraqi government, Iraq has primary jurisdiction over contractors and contractor employees that are working within

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<sup>352</sup> See the Montreux Document, 17–18.

<sup>353</sup> *Ibid.*, 19.

<sup>354</sup> *Ibid.*, 19–20.

<sup>355</sup> Brooks and Chorev, “Ruthless Humanitarianism: Why marginalizing private peacekeeping kills people,” 125.

Iraqi official territory as United States nationals, or third country nationals; however, the withdrawal agreement does not encompass persons or entities that normally reside in Iraq. On the other hand, Afghanistan theoretically reserves the right to prosecute contractors working on behalf of United States; however, in practice, if the personnel of PMCs employed by the United States commit crimes in Afghanistan, they are not subject to Afghanistan laws but to U.S. prosecution. This implication, similar to what happened in Iraq prior to 2009, is the natural outgrowth of institutional weakness of Afghanistan in the area of judiciary. Despite mutual agreements between the United States and the territorial countries, patches to international laws, and expansion of the UCMJ to cover contractors accompanying United States military in Iraq and Afghanistan, some private military personnel still remain outside the jurisdiction.<sup>356</sup>

*a. U.S. Law*

Normally, contractor personnel would be subject to the laws of the territorial state. PMCs usually operate in failed states, where justice systems, as any other institutions, do not work properly. In such cases, the responsibility falls to the contracting state; however, in some cases the application of contracting state laws is also problematic, since crimes are committed abroad.<sup>357</sup> In order to fulfill its non-transferable responsibility of improving the regulation of PMCs, the U.S legislative branch has taken many steps to address accountability and transparency problems regarding PMCs in contingency operations. Most significantly was the expansion of the UCMJ to encompass the staff of PMCs in contingency operations in 2007. In this context, the MEJA and the UCMJ seem promising in terms of regulation of PMCs in contingency operations.

Under the 2007 Defense Authorization Act, Congress expanded the UCMJ to cover civilian contractors who are performing tasks in contingency operations, such as Operation Iraqi Freedom (OIF), and Operation Enduring Freedom (OEF).<sup>358</sup> UCMJ Article 2 (a)(10) states that, “In time of declared war *or a contingency operation*, persons

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<sup>356</sup> Minow, “Outsourcing Power: Privatizing Military Efforts and the Risks to Accountability, Professionalism, and Democracy,” 118–122.

<sup>357</sup> Caparini, “Regulating Private Military and Security Companies: The US Approach,” 172.

<sup>358</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: legal issues,” 24.

serving with or accompanying an armed force in the field" are subject to UCMJ.<sup>359</sup> United States Code 101 defines "contingency operations as follows:

. . . a military operation that--

(A) is designated by the Secretary of Defense as an operation in which members of the armed forces are or may become involved in military actions, operations, or hostilities against an enemy of the United States or against an opposing military force; or

(B) results in the call or order to, or retention on, active duty of members of the uniformed services under section 688, 12301(a), 12302, 12304, 12305, or 12406 of this title, chapter 15 of this title, or any other provision of law during a war or during a national emergency declared by the President or Congress.<sup>360</sup>

Previously, civilians could only be prosecuted under the UCMJ in times of war. Now they are subject to the UCMJ even during contingency operations. However, expansion of the UCMJ has raised many issues; the most critical of which is whether it is appropriate to expose civilian contractors to the military justice system. Another issue that scholars often raise is whether the U.S. Congress has the authority to order the prosecution of civilians under military discipline. If we consider the answers to the previous issues as positive, who would be responsible to prosecute them? What will happen if the principal deliberately overlooks contractors' breaching of law? Finally, would civilian contractors also be subject to the articles in regard to command structure and military honor? Thus, confusion remains.

MEJA is another regulation that is useful in addressing the problem of how to deal with civilians that committed crimes while accompanying military operations abroad.<sup>361</sup> MEJA covers persons "employed by or accompanying the armed forces" overseas.<sup>362</sup> In this regard, MEJA covers private military personnel working for the

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<sup>359</sup> See Uniform Code of Military Justice (UCMJ) Article 2(a)(10), available at: <http://usmilitary.about.com/od/justicelawlegislation/a/ucmjart2.htm> (accessed July 28, 2010).

<sup>360</sup> See 10 U.S.C.101 (a)(13), available at: <http://law.justia.com/us/codes/title10/10usc101.html> (accessed July 28, 2010).

<sup>361</sup> Caparini, "Regulating Private Military and Security Companies: The US Approach", 179.

<sup>362</sup> See Military Extraterritorial Jurisdiction Act of 2000, P.L.106-523 114 Stat, 2488. Available at: <http://www.publaw.com/hi/pl106-523.pdf> (accessed July 28, 2010).

Department of Defense; however, it does not encompass private military personnel working for other agencies.<sup>363</sup> Persons who are nationals of or habitually residing in the host nation are also not covered by MEJA.<sup>364</sup> DoD Instruction 5525.11 was issued in 2005 to implement MEJA outside the United States.<sup>365</sup> This instruction obligates the DoD Inspector General to notify the Attorney General when DoD personnel commit a federal crime overseas.<sup>366</sup> Instruction 5525.11 also requires DoD Inspector General to be responsible for conducting investigations to put MEJA into effect.<sup>367</sup> Marina Caparini states that due to the limitations in MEJA, it can only be exercised only if DoD is the employer of the contractor, thus it has rarely been applied to contractors so far.<sup>368</sup>

***b. Iraqi Law***

According to Coalition Provisional Authority (CPA) Order Number 17, issued in 2003, coalition forces were immune from Iraqi prosecution if they committed crimes, as long as CPA was in power.<sup>369</sup> After the CPA handed over the rule of the country to the new Iraqi government in 2004, CPA Order Number 17 remained in place for a while. In the current situation, the government of Iraq reserves the authority to prosecute the contractors who work for U.S. agencies, the multinational forces and diplomatic entities, if they commit crimes in Iraqi official territory.<sup>370</sup> A withdrawal agreement, which was signed by the U.S. and Iraq on November 17, 2008, provides the

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<sup>363</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: legal issues,” 22.

<sup>364</sup> Ibid.

<sup>365</sup> Ibid.

<sup>366</sup> Ibid.

<sup>367</sup> Ibid.

<sup>368</sup> Caparini, “Regulating Private Military and Security Companies: The US Approach,” 180.

<sup>369</sup> See CPA Order 17, as amended June 17, 2004, at: [http://www.cpa-iraq.org/regulations/20040627\\_CPAORD\\_17\\_Status\\_of\\_Coalition\\_Rev\\_with\\_Annex\\_A.pdf](http://www.cpa-iraq.org/regulations/20040627_CPAORD_17_Status_of_Coalition_Rev_with_Annex_A.pdf). (accessed August 7, 2010).

<sup>370</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan: Legal Issues,” 11. Also see R. Chuck Mason, “U.S.-Iraq Withdrawal/Status of Forces Agreement: Issues for Congressional Oversight,” *CRS Report R40011*, July 13, 2009, 7–8.

Iraqi government with primary jurisdiction over non-Iraqi U.S. Defense contractors and their employees who normally reside in Iraq.<sup>371</sup> The Agreement defines contractors and contractor employees as follows:

non-Iraqi persons or legal entities, and their employees, who are citizens of the United States or a third country and who are in Iraq to supply goods, services, and security in Iraq to or on behalf of the United States Forces under a contract or subcontract with or for the United States Forces. However, the terms do not include persons or legal entities normally resident in the territory of Iraq.<sup>372</sup>

The withdrawal agreement does not obligate the Iraqi government either to negotiate with the United States how cases will be handled, or to notify the U.S. officials that a contractor has been taken into custody. Jennifer K. Elsea states that although the Withdrawal Agreement does not seem to encompass contractor employees working for agencies other than the Department of Defense, citizens of Iraq and persons habitually living in Iraq, Iraq has overall exclusive jurisdiction over these personnel, given that eventually all of these entities operate under Iraqi laws.<sup>373</sup> Conversely, the Withdrawal Agreement gives the United States authorization to arrest or detain contractor personnel, if they are caught within the boundaries of United States' bases. Nonetheless, in this case, the United States is obliged to notify of the arrest and to hand the captive over to Iraqi authorities within 24 hours.<sup>374</sup> In other cases, the United States has to get a warrant from an Iraqi court in order to arrest or detain a contractor.<sup>375</sup> Thus, the Withdrawal Agreement provides the government of Iraq with the necessary authorization to arrest or detain contractor personnel; however, the application of this agreement still seems problematic due largely to weak enforcement mechanisms in Iraq.

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<sup>371</sup> See the Agreement between the United States and the Republic of Iraq on the Withdrawal of United States Forces from Iraq and the Organization of Their Activities during Their Temporary Presence in Iraq, Article 12.2, 10. available at: [http://www.usf-iraq.com/images/CGs\\_Messages/security\\_agreement.pdf](http://www.usf-iraq.com/images/CGs_Messages/security_agreement.pdf), (accessed July 28, 2010). Also see Elsea, "Private Security Contractors in Iraq and Afghanistan," 13.

<sup>372</sup> Ibid., Article 2.5, 2.

<sup>373</sup> Elsea, "Private Security Contractors in Iraq and Afghanistan," 12.

<sup>374</sup> See the Agreement between the United States and the Republic of Iraq on the Withdrawal of United States Forces from Iraq and the Organization of Their Activities during Their Temporary Presence in Iraq, Article 12.5, 10–11. Also See Elsea, "Private Security Contractors in Iraq and Afghanistan," 12.

<sup>375</sup> Ibid., Article 22.4, 18.

*c. Afghanistan Law*

In Afghanistan, the United States supports two different military operations: Operation Enduring Freedom, and The International Security Assistance Force (ISAF). OEF is a United States-led coalition that embarked on its operations in Afghanistan in 2001. Alternatively, ISAF is a NATO-led coalition, which performs its mission under UN mandate. Accordingly, personnel of each mission operate under different agreements. While United States military and civilian personnel participating in OEF are subject to the security agreement between the United States and the Islamic Transitional Government of Afghanistan (ITGA), those who are working under ISAF are subject to the Military Technical Agreement.

According to the Military Technical Agreement, ISAF personnel, who are deployed under the UN mandate, have immunity from Afghan prosecution, and therefore are subject to the jurisdiction of their homeland countries.<sup>376</sup> In this respect, currently the U.S. has primary jurisdiction over its military and civilian personnel working under ISAF.

Conversely, the United States and ITGA signed a treaty in 2002 concerning the legal status of U.S. military and civilian personnel that are operating in Afghanistan.<sup>377</sup> This agreement exempts U.S. military and civilian personnel from Afghan prosecution if they commit crimes inside the course of their duties.<sup>378</sup> Similar to personnel working under ISAF, the United States is the primary authority to execute criminal jurisdiction over its own personnel operating under OEF in Afghanistan. The subsequently elected government, the Government of the Islamic Republic of

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<sup>376</sup> See the Military Technical Agreement, A-1. Available at: <http://webarchive.nationalarchives.gov.uk/+http://www.operations.mod.uk/isafmta.pdf> (accessed July 28, 2010). Also see Elsea, “Private Security Contractors in Iraq and Afghanistan,” 13.

<sup>377</sup> *Ibid.*, 12.

<sup>378</sup> Elsea, “Private Security Contractors in Iraq and Afghanistan,” 12.

Afghanistan, approved this agreement as well; therefore, the security agreement still remains in place.<sup>379</sup> Nevertheless, the security agreement does not seem to exempt contractor personnel from prosecution.<sup>380</sup>

## **C. OPTIONS FOR REGULATION**

### **1. International Level**

#### ***a. Applying State and Command Responsibility Doctrines***

In “Private Military Companies and International Law: Building New Ladders of Legal Accountability and Responsibility,” Maogato and Sheehy propose that two well-established doctrines of international law, state responsibility and command responsibility, can be used to increase the accountability of PMCs.<sup>381</sup> They examine the Abu Ghraib case to indicate how these doctrines can help better regulate PMCs, who have increasingly been contracted by the United States to implement strategic objectives. They conclude that breaches by employees of CACI and Titan Corporation, who were hired by United States government through a temporary contract, can be attributed to both the United States and the PMCs. While State responsibility doctrine may hold the United States responsible as a contracting state, command responsibility doctrine may hold not only United States, but also CACI and Titan Corporation responsible, since employees committed these crimes under the authority of military commanders via the chain of command in the U.S. military, and civilian superiors via chain of command within PMC.<sup>382</sup>

Normally, states have no responsibility over the activities of non-state actors and private persons or firms. International law does not attribute breaches by these

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<sup>379</sup> Michael John Garcia, R. Chuck Mason, “Congressional Oversight and Related Issues Concerning International Security Agreements Concluded by the United States,” CRS Report R40614, October 1, 2009, 17.

<sup>380</sup> Garcia and Mason, “Congressional Oversight and Related Issues Concerning International Security Agreements Concluded by the United States,” 17. See also Elsea, “Private Security Contractors in Iraq and Afghanistan,” 14.

<sup>381</sup> Maogato and Sheehy, “Private Military Companies and International Law: Building New Ladders of Legal Accountability and Responsibility,” 99.

<sup>382</sup> *Ibid.*, 126–127.



entities to states, because these non-state actors and private entities are not directly subject to international law. States, on the other hand, are the main subjects of international law. International law has created a doctrine over time called “state responsibility,” to cover these non-state actors and private entities, which temporarily perform delegated functions on behalf of states.<sup>383</sup> When these private actors become temporary agents of states through a contract, international law conceptualizes these non-state actors or private entities as “de facto agents” of states.<sup>384</sup> If there is some form of contract between a state and its temporary agent, state responsibility doctrine connects de facto agent’s misconduct or breach of international law to the state that contracted it.<sup>385</sup> Thus, states may be responsible for actions of their de facto agents.<sup>386</sup>

Command responsibility doctrine has widely been considered to be unique to the military, traditionally perceived as non-transferable responsibilities of commanders over crimes and violations of the subordinates under their control. However, today some international law specialists claim that in some situations, command responsibility doctrine should encompass non-military superiors as well. For example, according to Maogato and Sheehy:

. . . it is clear that under the existing international law doctrine of command responsibility, political, paramilitary and bureaucratic superiors may be held liable for a failure to control their subordinates . . . Although doctrine in various forms has existed for millennia with regard to military personnel, it has only recently become a doctrine of international law that extends to encompass civilian persons.<sup>387</sup>

Article 86 of Protocol I to the Geneva Conventions make superiors responsible for a breach by their subordinates. As paragraph 2 of the article states:

The fact that a breach of the Conventions or of this Protocol was committed by a subordinate does not absolve his superiors from penal or

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<sup>383</sup> Maogato and Sheehy, “Private Military Companies and International Law: Building New Ladders of Legal Accountability and Responsibility,” 109.

<sup>384</sup> Ibid.

<sup>385</sup> Ibid.

<sup>386</sup> Ibid., 110.

<sup>387</sup> Ibid., 118.

disciplinary responsibility, as the case may be, if they knew, or had information which should have enabled them to conclude in the circumstances at the time, that he was committing or was going to commit such a breach and if they did not take all feasible measures within their power to prevent or repress the breach.<sup>388</sup>

Article 87 of Protocol I to the Geneva Conventions extends command responsibility of commanders to encompass civilians under their control. As paragraph 1 of the article notes:

The High Contracting Parties and the Parties to the conflict shall require military commanders, with respect to members of the armed forces under their command and other persons under their control, to prevent and, where necessary, to suppress and to report to competent authorities breaches of the Conventions and of this Protocol.<sup>389</sup>

International Committee of the Red Cross (ICRC) commentaries on additional protocol articulates that command responsibility doctrine must be conceptualized in a way that covers both military commanders and civilian superiors, stating that “[t]he concept of the superior is broader and should be seen in terms of a hierarchy encompassing the concept of control.”<sup>390</sup> Therefore, as a matter of international law, command responsibility can be applied to superiors of PMCs as well as military commanders.

#### ***b. Creating a Registering Entity***

In his thesis, “Regulation of PMCs in Iraq,” Nihat Dumlupinar recommends that establishment of an international institution, which is authorized to give PMCs official licenses to operate abroad, will facilitate regulation.<sup>391</sup> He states that in addition to its primary mandate of providing PMCs with formal approval to perform their

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<sup>388</sup> See the Additional Protocol to the Geneva Conventions, Article 86, paragraph 2, at: <http://www.icrc.org/ihl.nsf/WebART/470-750112?OpenDocument> (accessed August 4, 2010)

<sup>389</sup> See the Additional Protocol to the Geneva Conventions, Article 87, paragraph 1.

<sup>390</sup> Yves Sandoz, Christopher Swinarski, and Bruno Zimmerman eds., *Commentary on the Additional Protocols of 8 June 1977 to The Geneva Conventions of 12 August 1949*, (Geneva: Martinus Nijhoff Publishers, 1987), 1013. At: [http://www.loc.gov/rr/frd/Military\\_Law/pdf/Commentary\\_GC\\_Protocols.pdf](http://www.loc.gov/rr/frd/Military_Law/pdf/Commentary_GC_Protocols.pdf) (Accessed on August 4, 2010).

<sup>391</sup> Dumlupinar, “Regulation of Private Military Companies in Iraq,” 91.

mission internationally, this institution may keep records of activities of PMCs that are registered, providing some form of institutional memory.<sup>392</sup> These records would not only help states better regulate PMCs, but also force PMCs to respect international norms while executing their missions.

*c. Enforcing International Law*

International law holds states responsible for breaches of their de facto agents. It mandates that states have non-transferable responsibilities such as taking the precautions in their power to prevent breaches by their de facto agents and punishing perpetrators. International law obligates states to make amendments to their existing regulations to facilitate prosecution, extend their jurisdictions to cover the personnel of their de facto agents operating overseas, establish effective oversight mechanisms to prevent abuses by them, and enforce laws immediately to deter potential misconduct or non-compliance with international norms. If they cannot punish perpetrators through their domestic laws, international law requires that they submit them to the International Criminal Court.

Any law that lacks a properly working enforcement mechanism is doomed to be breached. International law is no exception. Most of the challenges regarding international regulation can be attributed to the dysfunctional enforcement mechanism. Since there is no overarching authority to impose sanctions on PMCs and their personnel when necessary, PMCs often take advantage of this power vacuum to get unfair leverage over states, and sometimes breach international laws without any concern. PMCs also appropriate the impotence of failed states, where institutions are relatively weak, and where the very governance itself is problematic. In this regard, properly working international law with an effective enforcement mechanism is critical for these states to protect themselves from the potential hazards of careless utilization of PMCs by other states on their sovereignty.

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<sup>392</sup> Dumlupinar, "Regulation of Private Military Companies in Iraq," 91.

## **2. National Level**

States are not autonomous entities. Rather, they are composed of individuals, groups, and institutions with their own interests. These entities seek to influence state behavior according to their own driving incentives. Therefore, it is pretty difficult for these entities to reach a consensus. For this reason, even the most organized and capable states, like the United States, sometimes face challenges in taking corrective action. On the other hand, it is much more difficult for weak and failed states, such as Iraq and Afghanistan, to conciliate these distinct interests and reach an agreement.

### ***a. The United States***

Of these three countries, the United States is the most capable and most successful in terms of domestic regulation. Most of the good practices written in the Montreux Document are taken from the experiences of the United States in contingency operations in Iraq and Afghanistan. Despite some shortcomings and small defects, the United States has one of the most comprehensive regulatory frameworks with respect to PMCs. In the last few years, the United States Congress has adopted various measures to improve institutional oversight over the PMCs. The United States Congress expanded and clarified jurisdiction over crimes committed by private military personnel overseas. To some extent, these measures improved the regulatory framework in the United States; however, it appears that much remains to be done to make sure that offences by private military personnel do not go unpunished.

In the United States, there are many good practices with respect to utilization of PMCs. For instance, federal agencies generally repeat their contracts with cost-efficient and reputable PMCs, while staying away from PMCs that seek high value, high-risk, and single-shot contracts. In order to prevent information asymmetry in contingency operations, the United States also uses “fire-alarming” to get feedback about breaches and violations of PMCs that it contracted with, using the media, local people, local security forces, and NGOs that simultaneously use the same territory with PMCs. Fire-alarming creates an additional pressure on PMCs, obligating them to be careful not to undermine their reputation by poorly or inappropriately performing their functions. It

helps strengthen existing monitoring mechanisms, deterring PMCs from breaching international humanitarian law. Thus, fire-alarming systems facilitate regulation by encouraging PMCs to “self-report” their own actions. The United States also has effective institutional monitoring mechanisms, such as, GAO, CRS, SIGIR and SIGAR. These mechanisms provide the United States government and Congress vital information regarding PMCs. The United States also uses institutional checks like “judicial review” in order to control PMCs.

Nevertheless there are weaknesses in the existing regulations as well. Although the United States extended the UCMJ to encompass civilians who accompany United States military in contingency operations in 2007, some personnel still remain outside the jurisdiction and largely due to political unwillingness. The United States sometimes fails to enforce existing domestic laws and impose sanctions on PMCs when necessary. The United States has the most comprehensive regulation system with respect to PMCs; however, it can more effectively regulate the private military industry.

The first step for the United States must be to create a comprehensive doctrine that recognizes the significance of the presence of PMCs in contingency operations. Evaluating whether existing regulations are adequate for exerting control over PMCs in contingency operations and authorizing the legislative branch to take steps to improve domestic regulation to cover private military personnel remaining outside of the jurisdiction, the United States can better regulate PMCs. In doing that, the United States legislative branch can take the judiciary’s concerns and proposals into account.

Second, abstaining from outsourcing inherently governmental functions to PMCs, the United States can better protect its national interests abroad. Contracting out certain tasks, during the execution of which employees of PMCs are likely to use force, runs the risk of undermining the efforts of the United States in contingency operations.

Third, the United States can go on to promote the current licensing system to indirectly control the activities of PMCs that are registered in the United States but operate abroad. While providing PMCs with relevant licenses and authorizations, taking

the criminal records and past performances of PMCs into consideration may be useful for the United States to exert better control over PMCs. In this regard, improving SPOT is essential to increasing the accountability of PMCs.

***b. Iraq and Afghanistan***

Territorial states have also obligations regarding regulating PMCs in terms of international law. The Montreux Document states that territorial states should assess whether the internal legal framework is adequate to properly regulate PMCs that operate within their territories or whether it needs adaptations or amendments.<sup>393</sup> Iraq and Afghanistan face many challenges with regard to enforcing existing laws. Moreover, creating and enforcing additional laws may seem too difficult for these new governments. Although Both Iraq and Afghanistan have primary jurisdiction over the activities of PMCs within their territories, they lack mechanisms to punish perpetrators.<sup>394</sup> Democratic institutions in those countries are relatively new and weak, so it is pretty problematic for these countries to properly regulate PMCs alone. The Withdrawal Agreement provides the Iraqi government with the necessary authorizations to prosecute private military personnel.<sup>395</sup> Nonetheless, the application of this agreement still seems problematic, due largely to weak enforcement mechanisms in Iraq. In Afghanistan, the Military Technical Agreement provides the United States with the primary jurisdiction over its private military personnel who are deployed as ISAF personnel under the UN mandate.<sup>396</sup> Nominally, the government of Afghanistan has the primary authority to carry out criminal jurisdiction over private military personnel operating on behalf of the United States government under OEF, but in practice the only capable entity in the country that can prosecute the staff of PMCs is the United States. The Montreux Document

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<sup>393</sup> See the Montreux Document, 20.

<sup>394</sup> Caparini, "Regulating Private Military and Security Companies: The US Approach," 172.

<sup>395</sup> See the Agreement between the United States and the Republic of Iraq on the Withdrawal of United States Forces from Iraq and the Organization of Their Activities during Their Temporary Presence in Iraq, Article 12.2.

<sup>396</sup> See the Military Technical Agreement, A-1.

acknowledges these challenges and recommends territorial states to cooperate with the contracting state to better regulate PMCs operating in their territories.<sup>397</sup>

In this regard, in order to better regulate PMCs within their own territories, Iraq and Afghanistan may require PMCs to obtain official license or authorization from both their homeland governments and territorial state governments.<sup>398</sup> Criteria for official license may require PMCs to have sufficient economic and financial capacity with clear personnel and property records, and to employ well-trained personnel who have clear records. Territorial states must be careful about not to grant license to PMCs that acquired weapons illegally. The Montreux Document recommends territorial states that they should ensure that PMCs meet the following criteria, before getting relevant licenses and authorizations:

- a) no reliably attested record of involvement in serious crime (including organized crime, violent crime, sexual offences, violations of international humanitarian law, bribery and corruption) and, insofar as the PMSC or its personnel had engaged in past unlawful conduct, has appropriately dealt with such conduct, including by effectively cooperating with official authorities, taking disciplinary measures against those involved, and where appropriate and consistent with findings of wrongdoing, providing individuals injured by their conduct with appropriate reparation;
- b) conducted comprehensive inquiries within applicable law regarding the extent to which any of its personnel, particularly those who are required to carry weapons as part of their duties, have a reliably attested record of not having been involved in serious crime or have not been dishonorably discharged from armed or security forces;
- c) not previously had an operating license revoked for misconduct of the PMSC or its personnel.<sup>399</sup>

While granting official licenses and authorizations, territorial states may require PMCs to train their personnel sufficiently, implementing both pre-deployment training and ongoing training. They may also obligate PMCs and their subcontractors to

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<sup>397</sup> See the Military Technical Agreement, A-1.

<sup>398</sup> Ibid.

<sup>399</sup> See the Montreux Document, 22.

work in harmony with domestic and international law.<sup>400</sup> Moreover, they can establish oversight mechanism to monitor their activities, taking all precautions within their power to enforce it.

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<sup>400</sup> See the Montreux Document, 22.



## **V. CONCLUSION**

This thesis sought to analyze the issues concerning how to outsource, monitor, manage and regulate PMCs that have become an indispensable part of contingency operations, so that they can be properly utilized to fulfill United States' policy objectives overseas. In this respect, utilization of PMCs by United States governmental agencies was examined in two different contingency operations: Operation Iraqi Freedom and Operation Enduring Freedom. This thesis studied these cases for two reasons. First, the United States government, which is a prominent customer of the private military industry, stands out as a unique example in terms of utilization of PMCs in contingency operations because it has a relatively long tradition of and much experience in outsourcing PMCs. Second; Iraq and Afghanistan have become test areas with respect to the utilization of PMCs by governmental agencies to implement various contingency functions on behalf of the United States government. In this context, this conclusion will recap the arguments made in the previous chapters and provide overall considerations of how governmental agencies of the United States can better outsource, monitor, manage and regulate PMCs in contingency operations.

### **A. HOW TO BETTER OUTSOURCE PMCS**

The second chapter examined two primary factors that affect make-or-buy decisions of governmental agencies: transaction cost economics and inherently governmental functions. TCE was emphasized to better understand how transaction costs influence make-or-buy decisions of governmental agencies. This chapter argued that outsourcing has pushed both governmental agencies, which were formerly pure hierarchies, and PMCs, which previously only operated under market conditions, to adopt institutional structures of hybrid type of organizations. So, while governmental agencies have compromised some level of control and coordination in return for greater efficiency, PMCs have compromised some level of autonomy in exchange for the opportunities that the government agencies of the United States provided via contingency contracting. It was concluded that governmental agencies would be more likely to contract out a

particular function if this function does not reflect its core competency, if it does not rely on a highly specific asset, if uncertainty is low and if monitoring is easier. Otherwise, governmental agencies would more likely to keep the same function in-house, economizing on transaction costs.

The second chapter also analyzed inherently governmental functions to show how they affect make-or-buy decisions of governmental agencies. It was pointed out that inherently governmental functions aim to restrict governmental agencies from contracting out core or sovereign functions. It was demonstrated that hierarchies are better at protecting specific assets and carrying out sovereign functions that require considerable probity than are hybrids and markets. Therefore, this chapter recommended that it would be better for governmental agencies in the United States to not contract out inherently governmental functions in contingency operations, even if outsourcing them is more cost-efficient than keeping them in-house. It was noted that the application of this recommendation is, however, quite challenging, since there is no consensus on what those functions are.

Furthermore, TCE set forth three primary contractual hazards: asset specificity hazard, uncertainty hazard, and probity hazard. It was discussed that since some PMCs supply highly specific assets like sophisticated weapon systems and specialized human capital, they might pose serious dangers to the governmental agencies that depend on them. It was also argued that contracting with PMCs in contingency operations runs the risk of undermining the efforts of governmental agencies. Furthermore, it was emphasized that monitoring becomes harder in contingency operations for two reasons: because uncertainty is high and because PMCs have often incentives to hide information when they perform their missions geographically far from their principles. Finally, it was highlighted that probity hazard is also likely in contracts with PMCs in contingency operations because, unlike militaries, private security is not a profession. It was concluded that therefore, without effective monitoring and punishing mechanisms, abuses by PMCs cannot be prevented.

Finally, the second chapter asserted that outsourcing is a two-edged sword. Outsourcing some tasks to PMCs only when necessary may sometimes be cost-efficient

on the part of governmental agencies. Nonetheless, it may also be costly to utilize PMCs in contingency operations, especially when there are no effective monitoring mechanisms to supervise their activities.

## **B. HOW TO BETTER MONITOR AND MANAGE PMCS**

The third chapter sought to answer the question of how the United States might use oversight mechanisms to better manage PMCs in contingency operations. It was discussed that unless effective contract management and oversight mechanisms are established, costs might increase due to waste, corruption, and abuse. The third chapter revealed the dearth of required capacity in the United States to monitor PMCs, and the absence of commitment to supervise and manage contracts have played a key role in financial and conduct related abuses in Iraq and Afghanistan. New Institutionalism and Principal-Agent Theory provided the theoretical basis for this chapter. With respect to utilization of PMCs by governmental agencies in contingency operations, six major institutional problems were diagnosed. These institutional problems can be summarized as follows: doctrinal void and institutional misunderstanding of the roles that PMCs play in contingency operations, weaknesses in interagency coordination, shortage of contracting professionals, inadequate training of COs and CORs, unclear contracting requirements and immeasurable standards, and inadequate training of military commanders and personnel. In response to these six major institutional challenges, the third chapter proposed seven steps with regard to improving monitoring and managing of PMCs in contingency operations.

First, the development of a new doctrine that reflects organizational understanding of the roles that PMCs play in contingency operations is essential. This new doctrine must answer to the actual needs of contingency operations. The importance of writing a living doctrine that can answer to the actual needs of contracting in contingency operations was highlighted. It is argued that doctrines do very little if members of institutions do not apply these principles in their daily tasks. Second, improving the existing SPOT system is vital because without accurate data, governmental agencies cannot outsource, supervise and manage PMCs. Third, creating an open, transparent and competitive market is crucial, because PMCs can easily overcharge their

governmental agencies if there is no competitive market discipline. Markets can regulate PMCs, but only if they are open, transparent, and competitive. Fourth, strengthening interagency coordination mechanisms is critical. Governmental agencies that use PMC in contingency operations must not only coordinate with each other, but must also coordinate with other regional and international organizations and the governmental agencies of the territorial states that contract with PMCs. Better coordination would likely bring about greater efficiency and control, as well as less fraud, waste and abuse. Fifth, increasing the quality and quantity of contracting professionals is important because a greater number of contracting professionals with better training would presumably lead to better monitoring and contract management on the part of governmental agencies and less financial and conduct related abuses on the part of PMCs. Sixth, training military personnel and clarifying authorities are imperative. The third chapter discusses in detail that commanders on the battlefield often have no idea about whether and how they can manage PMCs. Much of this confusion derives from insufficient pre-deployment and ongoing training, and intricate lines of authority over PMCs. Elimination of this complication would predictably increase control over PMCs. Seventh, continuing to use a licensing system as an effective indirect mechanism to compel PMCs to respect international norms and standards is cardinal. In this respect, this chapter recommends the United States monitor PMCs that are registered in the United States but operate in Iraq and Afghanistan, even if they work independently from the United States government, that the U.S. cancel the licenses of those whose misconduct is proven.

### **C. HOW TO BETTER REGULATE PMCS**

In the fourth chapter, major challenges regarding the regulation of PMCs in contingency operations were reviewed to demonstrate how the current regulatory framework exempts some of the staff of PMCs from prosecution in Iraq and in Afghanistan. It was discussed that PMCs may undermine stabilization and reconstruction efforts when they are not regulated properly.

This chapter argued that even though there are international laws that seek to regulate PMCs, they do not define the current activities and roles of PMCs in contingency operations. Furthermore, the fourth chapter put forth that international law lacks enforcement mechanisms to prosecute offences by private military personnel, so cannot properly regulate PMCs in contingency operations alone. It was highlighted that domestic laws, not only in the United States but also in Iraq and Afghanistan, are unable to regulate PMCs effectively, either because of insufficient capacity or because of political unwillingness. Thus, chapter four maintained that enforcement problem of the international law, insufficient capacity of Iraq and Afghanistan, and political unwillingness of the United States, provided PMCs with considerable flexibilities in terms of their legal obligations and practices in contingency operations.

It was also discussed in the fourth chapter that the complexity of prosecuting private military personnel operating in contingency operations is due largely to their vague legal status under international law. It was clarified that even though PMCs themselves do not have a status under international humanitarian law, their employees do. It was stated that the status of the staff of PMCs, however, is contingent on the nature of their contract and the nature of functions they perform, so must be determined on a case-by-case basis. The fourth chapter proposed that as a matter of international law, state responsibility and command responsibility doctrines can be applied to PMCs as well as states to increase the accountability of PMCs in contingency operations. In addition, it was recommended that the establishment of an international institution that is authorized to give PMCs official licenses to operate abroad would facilitate regulation. Finally, it was noted that this institution may keep records of PMCs, providing governmental agencies with vital institutional memory and pushing PMCs to respect international norms while executing their missions.

The fourth chapter also argued that states are not autonomous entities, but are made up of individuals, groups, and institutions that seek to influence the state behavior in accordance with their distinct motives and interests. It was claimed that reaching a consensus to take corrective action is therefore a big challenge, even for well-organized and capable states. In this regard, the fourth chapter suggested that the United States,

Iraq, and Afghanistan use the Montreux Document as a guide to better regulate PMCs in contingency operations. It was emphasized that cooperation between these states is essential for a more effective regulation. Finally, it was recommended that keeping their non-transferable responsibilities under international law, these states should take all measures in their power to implement as many best practices written in the document as possible to exert better control over PMCs in contingency operations.

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